

HAWAII ADMINISTRATIVE RULES

TITLE 16

DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS

CHAPTER 38

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SUBCHAPTER 1

GENERAL PROVISIONS

§16-38-1 Definitions. As used in this chapter, and in the forms, instructions, and orders of the commissioner of securities, the following meanings shall apply to the extent that they are not inconsistent with the definitions provided by section 485-1, HRS:

"Affiliate" means a person who directly or indirectly, through one or more intermediaries, controls, or is controlled by, or is under common control with another person.

"Amount" means the aggregate dollar value affixed to the shares. In context with capitalization: number of shares X par or stated value = amount. In context with offering: number of shares X offering price per unit = amount.

"Applicant" means the issuer, dealer, investment adviser, or other person executing the application.

"Application" means the form prescribed by the commissioner and including any other paper or document filed pursuant to chapter 485, HRS, in connection with the registration of a security or the registration of a dealer or salesperson, including all amendments, papers, documents, and exhibits incidental thereto.

"Certificate of interest or participation in any profit-sharing agreement" shall not include any interest in a general partnership or joint venture where the interest is not assignable without the consent of all the other members and where all the members participate directly in managing the partnership or joint venture.

"Commissioner" means the director of commerce and consumer affairs of the State of Hawaii who is ex-officio the commissioner of securities.

"Control" or "controlling person" means possession of the power, authority, or means to engage in the management or policymaking functions of a person, directly or indirectly, through ownership of securities, by contract or otherwise. A person owning at least twenty-five per cent of the outstanding voting securities of another shall be presumed to be a "controlling person." Any presumption may be rebutted by evidence but shall continue until a determination to the contrary has been made by the commissioner.

"Insider" means every controlling person of another, including every officer, director, partner or trustee, or individual occupying similar status or

performing similar functions, and every promoter (if the organization took place within three years from date of application).

"Institutional buyer." For purposes of section 485-6(8), HRS only, "institutional buyer" includes any organization within the scope of section 501(c)(3) of the Internal Revenue Code of 1954, as amended.

"Investment adviser." For purposes of section 485-1(6), HRS only, an "investment adviser" is any person, corporation, partnership, or other unincorporated association that receives compensation, directly or indirectly for the rendering of investment advisory services whether by salary, flat fee, or by periodic retainer fees.

"Investment advisory contract" includes, but shall not be limited to, the advice, recommendations or services of the investment adviser in regards to the following:

- (1) Any interest or participation in a contract, transaction, scheme, common enterprise, or profit-seeking venture whereby the investor transfers capital to the investment adviser or invests pursuant to the investment adviser's advice;
- (2) Any investment by which a client furnishes initial value to an investment adviser and a portion of this initial value is subjected to the risks of the enterprise, and the furnishing of the initial value is induced by the investment adviser's promises or representations which give rise to a reasonable understanding that a valuable benefit of some kind over and above the initial value shall accrue to the client as a result of the operation of the enterprise, and the client does not receive the right to exercise practical and actual control over the managerial decisions of the enterprise; and
- (3) Any investment with regard to completion costs of any oil, gas, or other mineral lease, right, or royalty.

"Investment advisory services" means activities that are conducted pursuant to an investment advisory contract for the purposes of effecting the terms of the contract.

"Isolated transaction" means a sale of a security or securities, whether effected through a dealer or not, where the number of persons solicited in this State in any one twelve-month period on behalf of the seller with respect to the securities shall not exceed twenty-five.

"Issuer." For the purposes of section 485-(11), HRS only, the term "issuer" includes security holders of a wholly owned subsidiary of the issuer.

"NASD" means the National Association of Securities Dealers, Inc.

"Officer" means a president, vice president, secretary, treasurer, or any other person performing similar functions with respect to any organization, whether incorporated or unincorporated.

"Organization" means a corporation, partnership, trust, association, joint venture, or syndicate.

"Parent" means an affiliate controlling another person.

"Predecessor" means a person, a major portion of whose business, assets, or control has been acquired by another.

"Promoter" means a person who, acting alone or in conjunction with others, takes the initiative in founding, organizing, or incorporating the business or enterprise of an issuer.

"Prospectus" means a document meeting the applicable requirements of chapter 485, HRS.

"Public offering" means any security offered for sale to the general public:

- (1) If it is advertised for sale in any newspaper, magazine, periodical, or other publication, or by means of a prospectus, offering circular, pamphlet, brochure, dodger, or addressed or unaddressed written or printed communication intended for public distribution or information; or
- (2) Where solicitation is made by billboard, window display, or use of phonographic or other recording, radio, television, or any public demonstration or explanation by any similar device.

"Registrant" means an applicant whose registration of securities has become effective under chapter 485, HRS.

"Registration statement" means the application for registration of securities after the registration thereby has become effective.

"Sale." For purposes of section 485-1(10)(B), HRS only, any offer or sale of a security issued by a wholly owned subsidiary to the shareholders of its parent in a non-taxable reorganization within the meaning of the Internal Revenue Code is not a sale.

"Salesperson" includes all salesmen under chapter 485, HRS. An officer of a corporation who transmits a prospectus in an exchange offering to stockholders in this State and who does not actively solicit offers is not a salesperson.

"SEC" means the Securities and Exchange Commission.

"Section 485-6(9), HRS," means that within twelve months after an organization is formed, the total number of subscribers of a preorganization certificate or subscription as set forth in section 485-6(10), HRS, plus the subsequent offerees, if any, after the organization is formed, of the same class of securities shall not exceed twenty-five.

"Share" means a share of stock or unit of investment in a corporation, or a unit of interest in an unincorporated person.

"Subsidiary" means an affiliate controlled by another person.

"Underwriter" means a dealer who participates in the distribution of a security, in connection with a public offering, either as a purchaser with a view to offer for resale, or one who undertakes to offer or sell, directly or indirectly, for an issuer. [Eff 6/4/70; am and ren §16-38-1, 7/30/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-1, 485-6)

§16-38-2 Filing. A document is filed when it is received in the office of the commissioner of securities.

All communications shall be addressed to: Commissioner of Securities, P.O. Box 40, Honolulu, Hawaii 96810; or deliver to: 1010 Richards Street, Honolulu, Hawaii.

The office of the commissioner of securities shall be open for transaction of business between the hours of 7:45 a.m. and 4:30 p.m. on weekdays, except legally declared holidays.

Only the original of each form or exhibit shall be required, unless otherwise provided in the form. [Eff 6/4/70; am and ren §16-38-2, 7/30/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§80-1, 485-2)

§16-38-3 Fees. The following fees shall be submitted with the application:

- (1) The fee for registration of securities by qualification shall be one-tenth of one per cent of the aggregate offering price of the securities to be offered in the State; minimum, \$20; maximum, \$200; renewal, \$20;
- (2) The fee for registration of securities by notification shall be one-twentieth of one per cent of aggregate offering price of the securities to be offered in the State; maximum, \$100;
- (3) The fee for registration of dealers shall be \$50 (original and renewal);
- (4) Registration by investment advisers shall be \$50 (original and renewal);
- (5) The fee for registration of securities salesperson shall be \$10 (original, reapplication, and renewal);
- (6) The fee for the securities salesperson examination shall be \$10;
- (7) The fee for registration of investment adviser representatives shall be \$10 (original, reapplication, and renewal);
- (8) The fee for the investment adviser representative examination shall be \$50;
- (9) The fee for the investment adviser examination shall be \$100; and

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- (10) The fee for copies of documents filed in the office of the commissioner shall be \$.50 cents per page. [Eff 6/4/70; am 5/27/80; am and ren §16-38-3, 7/30/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-9, 485-10, 485-11, 485-14)

§16-38-4 Forms. Typewritten or photocopied reproductions of the following forms shall be accepted:

- S-1 Application for registration of securities by qualification (U-1 form as adopted by the National Association of Securities Administrators (NASA) may be used in place of this form;
- S-3 Consent to service of process by issuer of, dealer or investment adviser in securities (U-2 form as adopted by the NASA may be used in place of this form);
- S-4 Resolution authorizing consent to service of process (U-2A form as adopted by the NASA may be used instead of this form);
- S-5 Bond for dealer in, issuer of or investment adviser in securities;
- S-6 Application for registration as a dealer in securities;
- S-7 Application for renewal of registration as a dealer in securities for the period ending December 31, 19__;
- S-8 Application for registration as securities salesperson;
- S-9 Application for renewal of registrations of securities salespersons for the period ending December 31, 19__;
- S-10 Reapplication for registration of securities salesperson;
- S-11 Application for re-examination of securities salesperson;
- S-12 Application for exemption from the registration requirement of the Hawaii Sale of Securities Act in order to offer or sell securities of residential cooperative corporation;
- S-13 Application for registration as an investment adviser in securities;
- S-14 Application for renewal of registration as an investment adviser in securities for the period ending December 31, 19__;
- S-15 Application for re-examination for investment adviser in securities;
- S-16 Bond for investment adviser in securities;
- S-17 Application for registration as an investment adviser representative;
- S-18 Application for renewal of registration(s) of investment adviser representative(s) for the period ending December 31, 19__;
- S-19 Reapplication for registration of investment adviser representative in securities;
- S-20 Application for re-examination of investment adviser representative. [Eff 6/4/70; am and ren §16-38-4, 7/30/81; am and comp 10/12/85]

(Auth: HRS §§91-2, 485-2) (Imp: HRS §§485-10, 485-11, 485-12, 485-14)

SUBCHAPTER 2

DEALERS

§16-38-5 Registration; generally. An applicant may be registered under chapter 485, HRS, if the commissioner finds that the applicant is qualified, has sufficient training and experience, is of good repute, and otherwise satisfies the requirement of chapter 485, HRS, and this chapter. [Eff 6/4/70; am and ren §16-38-5, 7/30/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-5.1 Registration; eligibility requirements. (a) An applicant, if a natural person, shall have attained the age of nineteen years.

(b) An applicant shall have a minimum capital as provided in section 16-38-5.3(b) of not less than \$5,000.

(c) A partner or an officer of a registered dealer or issuer may engage in the capacity of a salesperson only if that person has been duly registered as provided by section 485-14, HRS.

(d) In the case of a foreign corporation or a partnership intending to establish a branch in Hawaii, compliance shall be made with the requirements of the Hawaii foreign corporation law (chapter 418, HRS) or the Hawaii partnership law (chapter 425, HRS), respectively.

(e) A person shall not be registered as a dealer and salesperson concurrently. [Eff 6/4/70; am 1/1/71; am and ren §16-38-5, 7/30/81; am, ren §16-38-5.1 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-5.2 Registration; application. (a) An application for original or renewal registration shall be filed on a form prescribed by the commissioner or, in the case of an original application, on a form approved by the Securities and Exchange Commission and the State, and contain the information requested concerning the applicant's identification, qualification, business association, history, repute, experience, and financial condition.

(b) The application shall be filed together with the filing fee of \$100 and consent to service of process, \$5,000 bond, or cash or securities in lieu thereof, a verified balance sheet as of a date within thirty days of filing, or if the

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applicant has been engaged in business one year or more preceding, a balance sheet certified by an independent public accountant as of the last fiscal year, together with a balance sheet verified by the applicant as of a date within thirty days of filing.

(c) Additional exhibits or information not specifically required by the application but essential to a full presentation of all material facts relating to applicant's qualification shall be furnished properly identified.

(d) The commissioner may examine the applicant and require additional information which the commissioner deems appropriate in consideration of the applicant's eligibility for registration.

(e) An applicant for renewal of registration need not furnish the identical information schedules or exhibits submitted in connection with an original application, unless there has been a change in circumstances affecting previous disclosures or the data is specifically requested by the commissioner. [Eff 6/4/70; am 1/1/71; am and ren §16-38-5, 7/30/81; am, ren §16-38-5.2 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-5.3 Registration; financial requirements. (a) Every dealer currently registered shall file an annual report of condition within ninety days following the end of the calendar or fiscal year adopted as follows:

- (1) Dealers registered with the SEC shall file a copy of the financial report filed with the SEC; and
- (2) Dealers not registered with the SEC shall file a balance sheet, including analysis of surplus, certified by an independent public accountant in conformance with generally accepted accounting principles. Any statement which does not adequately reflect the applicant's true financial picture shall not be accepted.

(b) Within twelve months after the effectiveness of this chapter, each registered dealer shall have at all times a minimum net capital of not less than \$5,000 which as used in this section shall mean net worth, or the difference between total assets and total liabilities or indebtedness, after adjustment to eliminate or revise assets of doubtful or uncertain value and to reflect true liabilities, in accordance with the following schedule:

- (1) Asset items not allowable:
 - (A) Furniture, fixtures and equipment; and
 - (B) Intangible items, such as goodwill, prepaid preincorporation or organizational expenses, etc.;
- (2) Asset items to be adjusted or substantiated:
 - (A) Securities owned shall be adjusted to market value;

- (B) Value of real estate shall be attested to by qualified and disinterested persons;
- (C) Property in joint ownership shall be limited to applicant's interest therein; and
- (D) Value of unsecured notes, accounts receivable, or advanced commissions due from a salesperson, officer, director, partner, or affiliate may be required by the commissioner to be substantiated by an opinion of a bank, finance company, or other lending institution satisfactory to the commissioner. [Eff 6/4/70; am 1/1/71; am and ren §16-38-5, 7/30/81; am, ren §16-38-5.3 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-5.4 Books and records. (a) Every dealer shall make and keep the following books and records, which shall be maintained and preserved for a period of at least three years and made available for inspection by the commissioner upon reasonable notice. This chapter shall not require a member of a national securities exchange to make or keep the records of transactions cleared for a member by another member as are made and kept by the clearing member.

(b) Blotters (or other records or books of original entry) containing an itemized daily record of:

- (1) Purchases and sales of securities;
- (2) Receipts and deliveries of securities;
- (3) Receipts and disbursements of cash;
- (4) All other debits and credits; and
- (5) Each transaction, reflecting:
 - (A) The account or name of customer;
 - (B) Name and amount of securities;
 - (C) Certificate number, if any;
 - (D) Unit and aggregate purchase or sale price;
 - (E) Trade date; and
 - (F) Name or other designation of person from whom purchased or received, or to whom sold and delivered;

shall be kept.

- (c) Ledgers, reflecting:
 - (1) Assets and liabilities;
 - (2) Income and expenses;
 - (3) Capital accounts;
 - (4) Securities in transfer;
 - (5) Dividends and interest received;

- (6) Securities borrowed and loaned;
- (7) Monies borrowed and loaned, and collateral used or substituted therefor;
- (8) Securities failed to receive and failed to deliver; and
- (9) A record of all puts, calls, spreads and straddles and other options in which dealer has any direct or indirect interest, or which it has granted or guaranteed, containing at least:
 - (A) Identification of the security; and
 - (B) Number of units involved;

shall be kept.

(d) Ledger accounts, itemizing separately as to each cash or margin account of every customer and of the dealer, including employees and partners thereof:

- (1) Name and address of the beneficial owner of the account;
- (2) In the case of a margin account, the signature of the owner, or person authorized to transact business for the account;
- (3) Purchases and sales;
- (4) Receipts and deliveries of securities; and
- (5) All other debits and credits to the account;

shall be kept.

(e) Securities records, reflecting for each security (including securities in safekeeping) carried by the dealer for its account, or for the accounts of its customers, employees, or partners:

- (1) Clearance dates of all long and short positions;
- (2) Location of all securities long and offsetting position to all securities short; and
- (3) Name or designation of the account in which each position is carried;

shall be kept.

(f) Memorandum, of the following:

- (1) Each brokerage order for the purchase or sale of a security showing:
 - (A) Any instruction given or received, whether executed or unexecuted;
 - (B) Terms and conditions or instructions, and any modification or cancellation thereof;
 - (C) Account for which entered;
 - (D) Date and time of entry, and time of execution or cancellation, to the extent feasible;
 - (E) Price at which executed; and

- (F) Orders entered pursuant to the exercise of discretionary authority so designated;
- (2) Each purchase and sale for the account of the dealer, including employees and partners thereof, showing:
 - (A) Name of purchaser or seller;
 - (B) Price; and
 - (C) Date and time of execution;

shall be kept.

(g) Confirmations of all purchases and sales of securities and notices of all other debits and credits for securities, cash, and other items for the account of customers, partners, and employees shall be given or sent to persons at or before completion of each transaction, copies to be retained by the dealer disclosing, at least:

- (1) The account for which entered;
- (2) Instructions, terms and conditions, whether executed or unexecuted;
- (3) Date of execution of transaction (Time of trade shall be furnished upon request.);
- (4) Whether the dealer is acting as agent or as dealer for its own account; and
- (5) If dealer is acting as agent for the customer, the following information or, a statement that same shall be furnished upon request:
 - (A) The name of the person from whom the security was purchased, or to whom it was sold, and date and time the transaction occurred; and
 - (B) Source and amount of commission or remuneration received or to be received in connection with the transaction. [Eff 6/4/70; am 1/1/71; am and ren §16-38-5, 7/30/81; am, ren §16-38-5.4 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-16)

§16-38-5.5 Registration; post-effective requirements. (a) Upon acceptance of the application by the commissioner, a certificate of registration shall be issued certifying that the dealer is authorized to engage in the securities business in the State.

(b) Every registrant shall immediately notify the commissioner in writing of any material change in any information, exhibits, or schedules submitted, or circumstances disclosed in its last prior application, and a correcting amendment shall be filed at the time of occurrence or discovery of the changes, which include, but are not limited to the following:

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- (1) Change in firm name, ownership, management, or control of a dealer;
- (2) A change in any of its partners, officers, or persons in similar positions;
- (3) Change in its business address, or the creation or termination of a branch office in Hawaii;
- (4) Change in type of entity, general plan, or character of dealer's business, method of operation or type of securities in which it is dealing or trading;
- (5) Material adverse change in financial condition, insolvency, dissolution or liquidation, or impairment of working capital, or noncompliance with the minimum capital or bond requirements provided in sections 16-38-5.2(b) and 16-38-5.3(b);
- (6) Termination of business or discontinuance of those activities as a dealer or salesperson;
- (7) The filing of a criminal charge or civil action against a registrant or a partner or officer, in which a fraudulent, dishonest, or unethical act is alleged, or a violation of a securities law or any aspect of the securities business is involved; and
- (8) Entry of a court or administrative order or proceeding against a registrant to deny, suspend, or revoke a registration, or threatening to do so, or to enjoin it from engaging in or continuing any conduct or practice in the securities business, or to impose a fine, suspension, or expulsion from the NASD. [Eff 6/4/70; am 1/1/71; am and ren §16-38-5, 7/30/81; am, ren §16-38-5.5 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-5.6 Registration; expiration, renewal, termination. (a) All registrations shall automatically expire on December 31 of each odd-numbered year (unless sooner terminated) and shall be renewed not earlier than November 1 or later than December 1 of each odd-numbered year for the next two calendar years by filing the application for renewal, together with the application for renewal of registration of securities salespersons, with the renewal fees. Applications not received by December 1 shall be subject to a penalty of one hundred per cent of the renewal fee.

(b) Where registrations are permitted to expire without the filing of a renewal therefor, a subsequent application shall be considered in all respects as an original application.

(c) Registration may be terminated prior to the expiration date by filing a request for cancellation, together with the certificate of registration of a dealer

and certificates of registration of the salespersons. [Eff 6/4/70; am 1/1/71; am and ren §16-38-5, 7/30/81; am, ren §16-38-5.6 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

SUBCHAPTER 3

SALESPERSONS

§16-38-6 Registration; generally. A person may be registered as a securities salesperson under chapter 485, HRS, if the commissioner finds that the applicant is of good repute and otherwise satisfies the requirements of chapter 485, HRS, and this chapter. [Eff 6/4/70; am 5/27/80; am and ren §16-38-6, 7/30/81; am 11/5/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-6.1 Registration; eligibility requirements. (a) An applicant, if a natural person, shall have attained the age of eighteen years.

(b) An applicant shall be appointed by a registered dealer or issuer who shall state that the registered dealer or issuer believes the information in the application is true and complete.

(c) A salesperson may not be registered for more than one dealer or issuer at any time. [Eff 6/4/70; am 5/27/80; am and ren §16-38-6, 7/30/81; am 11/5/81; am, ren §16-38-6.1 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-6.2 Registration; application. (a) An application for original registration shall be filed on a form prescribed by the commissioner and contain the information required therein concerning the applicant's qualification and repute.

(b) The commissioner may make the examination of the applicant and require additional information deemed appropriate in the consideration of the applicant's eligibility for registration.

(c) A salesperson's application which has been on file for a period of ninety days with no attempt by the applicant to pass the qualifying examination shall be automatically withdrawn. [Eff 6/4/70; am 5/27/80; am and ren §16-38-6, 7/30/81; am 11/5/81; am, ren §16-38-6.2 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

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§16-38-6.3 Registration; examination requirements. (a) Unless specifically exempt every applicant for registration as a securities salesperson shall be required to pass a written examination in order to test the applicant's knowledge of the securities business. The passing score shall be seventy per cent for part I and seventy per cent for part II.

(b) An examination shall consist of two parts: part I furnished by the New York Stock Exchange covering securities in general; and part II shall be the Uniform Securities Agent State Law Examination (USASLE) administered by the NASD.

(c) The examination requirement for the general securities examination (part I) may be waived by proper showing or certification that an applicant:

- (1) Has passed the NASD or SEC examination not more than two years immediately preceding the date of filing; or
- (2) Has passed the general securities examination given by the New York Stock Exchange not more than two years immediately preceding the date of filing; or
- (3) Has passed the same examination in another state with the same passing grade as Hawaii not more than two years immediately preceding the date of filing; or
- (4) Has been previously registered as a securities salesperson, provided that the applicant's last effective registration in this State or elsewhere, was not more than two years immediately preceding the date of filing.

(d) The examination requirement for part II may be waived by proper showing or certification that not more than two years immediately preceding the date of filing, the applicant passed the USASLE with a score of seventy per cent or better or has been previously registered as a securities salesperson, provided that the applicant's last effective registration in this State or any other state, territory, or possession of the United States, as well as the District of Columbia and Puerto Rico, was not more than two years preceding the date of filing. An applicant claiming exemption of the part II examination shall also file a certification on a form provided by the commissioner stating that the applicant has read and understands chapter 485, HRS, and this chapter.

(e) Applicants who are only exempt from taking one part of the examination shall pass the remaining part of the examination.

(f) Applications submitted by applicants of non-NASD member firms or applicants of issuers (Oahu applicants only) shall be received together with the part I examination fee of \$10 by the respective closing dates. Examinations shall be given in the examination room of the department of commerce and consumer affairs, 1010 Richards Street, Honolulu, Hawaii. Dealers and issuers shall be notified by letter of the grades received by their applicants. Applicants who pass

the examination and are otherwise qualified shall be registered as securities salespersons upon receipt of the registration fee of \$10, which shall be paid within one hundred twenty days after notification that an applicant has passed the examination. Applicants who do not pay the registration fee within the one hundred twenty day period shall have their application canceled and shall file another application. Applicants who are unsuccessful in passing the examination may file an application for re-examination before the next closing date, together with the examination fee of \$10. The part I score shall only be valid for a period of two years.

(g) Applicants of non-NASD member firms or applicants of issuers who reside on the neighbor islands may take the part I examination on their respective islands and the examination dates shall be set after the application is filed. The requirements listed in subsection (f) pertaining to the payment of the registration fee shall also apply to applicants who reside on the neighbor islands.

(h) Applicants who have passed the NASD examination shall submit a copy of the "Notice of Acceptance" sent to the dealer by the NASD. Applicants who have passed the USASLE examination shall submit a copy of notification of grade results and certificate, on a form provided by the commissioner, stating that they have read and understand chapter 485, HRS, and this chapter.

(i) Applicants who subsequently pass both examinations and are otherwise qualified shall be registered as securities salespersons upon receipt of the registration fee of \$10 which shall be paid within one hundred twenty days after notification that they have passed both examinations. Applicants who do not pay the registration fee within the one hundred twenty day period shall have their applications canceled and shall file new applications and meet all licensure requirements.

(j) Any securities salesperson whose registration lapses for two years or more before applying for registration shall be required to apply as a new applicant.

(k) A schedule of closing and part I examination dates shall be mailed to each dealer and issuer prior to the start of every calendar year. [Eff 6/4/70; am 5/27/80; am and ren §16-38-6, 7/30/81; am 11/5/81; am, ren §16-38-6.3 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-6.4 Registration; post-effective requirements. (a) Upon completion of the application, compliance with the examination requirement, and acceptance by the commissioner, registration shall become effective and a certificate of registration (white copy) shall be issued certifying the authority for the securities salesperson to engage in the securities business on behalf of the dealer or issuer

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designated thereon. The blue copy of the certificate shall be retained by the dealer or issuer.

(b) The salesperson's certificate of registration shall be carried by the applicant at all times when engaged in the securities business and shall be presented upon request.

(c) Every registrant shall immediately notify the commissioner of the filing of a criminal charge or civil action in which a fraud, dishonest, or unethical action is alleged or a violation of the securities law is involved. [Eff 6/4/70; am 5/27/80; am and ren §16-38-6, 7/30/81; am 11/5/81; am, ren §16-38-6.4 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-6.5 Registration; expiration, renewal, termination. (a) All registrations shall automatically expire on December 31 of each odd-numbered year, unless sooner terminated, and shall be renewed by the dealer or issuer employing the salesperson not earlier than November 1 or later than December 1 of each odd-numbered year for the next two calendar years by filing an application for renewal of securities salesperson together with the renewal fee. Applications not received by December 1 shall be subject to a penalty of one hundred per cent of the renewal fee.

(b) Where registrations are permitted to expire without the filing of a renewal therefor, a similar application may be permitted to be filed within two years from the date of expiration on the form - reapplication for registration of securities salesperson. Applications filed after two years from the termination date shall be considered as original applications.

(c) A salesperson's certificate of registration may be terminated prior to its expiration date by either the dealer or issuer employing the salesperson or by the salesperson. A dealer or issuer may terminate the registration of any salesperson by filing a notice of termination with the commissioner together with the salesperson's certificate of registration (white copy). Termination shall be effective when the notice of termination is received by the commissioner.

(d) A salesperson's certificate of registration shall not be transferred. When a salesperson terminates connection with a dealer or issuer with whom the salesperson is registered, and wishes to be employed by another dealer or issuer, a notice of termination shall be filed with the commissioner together with the salesperson's certificate of registration (white copy). The salesperson may then reapply for registration with the new dealer or issuer by filing the form - reapplication for registration of securities salesperson. The form shall be endorsed by the new dealer or issuer.

(e) Termination of any dealer's or issuer's registration for any reason shall automatically constitute cancellation of all salespersons registered thereunder.

(f) When a salesperson ceases those activities of a salesperson, or the salesperson otherwise becomes ineligible to be registered, notice shall be promptly filed by the issuer or dealer for whom the subject is registered and the salesperson's certificate of registration shall be surrendered to the commissioner. In no event shall the notice be later than ten days following the event or occurrence. The notice shall be in letter form. [Eff 6/4/70; am 5/27/80; am and ren §16-38-6, 7/30/81; am 11/5/81; am, ren §16-38-6.5 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

SUBCHAPTER 4

DENIAL OF APPLICATION, SUSPENSION, AND REVOCATION OF REGISTRATION OF DEALERS, SALESPERSONS, INVESTMENT ADVISERS, AND INVESTMENT ADVISER REPRESENTATIVES

§16-38-7 Denial, suspension, and revocation. (a) A proceeding to deny, suspend, or revoke the effectiveness of an application or registration may be instituted by the commissioner if the action is in the public interest and if reasonable grounds exist that the applicant or registrant has violated or failed to comply with any provision of chapter 485, HRS, or this chapter.

(b) Without in any way limiting the generality thereof, for the purposes of section 485-15(4), HRS, any of the following shall demonstrate an applicant's or registrant's unworthiness to transact the business of a dealer or salesperson:

- (1) Causing unreasonable delay or failure to execute orders, liquidate customers' accounts, or in making delivery of securities purchased or remittances (or credit) for securities sold;
- (2) Selling securities at unfair prices in relation to market value, or with unreasonable or excessive markups or commissions;
- (3) Effecting transactions in the account of a customer without the customer's knowledge or consent or maintaining discretionary accounts without written authorization;
- (4) Wilful switching, churning, overtrading, or reloading of securities in a customer's account for the ostensible purpose of accumulating or compounding commissions;
- (5) Inducing a customer to invest beyond the customer's known immediate financial resources, or without regard to the nature and character of the account;
- (6) Engaging or aiding in "boiler room" operations or high-pressure tactics in connection with the promotion of speculative offerings or

"hot-issues" by means of an intensive telephone campaign or unsolicited calls to persons not known by, nor having an account with the salesperson or dealer represented by the applicant, whereby the prospective purchaser is encouraged to make a hasty decision to buy, irrespective of the prospective purchaser's investment needs and objectives;

- (7) Participating in the solicitation or offer for sale of promotional securities without the use and dissemination of a prospectus (where required), or making oral or written statements contrary to or inconsistent with the disclosures contained therein;
- (8) Making false, misleading, deceptive, exaggerated, or flamboyant representations or predictions in the solicitation or sale of a security:
 - (A) That the security shall be resold or repurchased; or
 - (B) That the security shall be listed or traded on an exchange or established market; or
 - (C) That the security shall result in an assured, immediate or extensive increase in value, future market price, or return on investment; or
 - (D) With respect to the issuer's financial condition, anticipated earnings, potential growth, or success; or
 - (E) That there is a guarantee against risk or loss;
- (9) Failing to disclose a dual agency capacity or effecting transactions upon terms and conditions other than those stated per confirmations;
- (10) Failing to make a bona fide public offering pursuant to an underwriting agreement or entering into an arrangement which establishes unfair or unreasonable terms and conditions or compensation;
- (11) Establishing fictitious accounts in order to execute transactions which would otherwise be prohibited;
- (12) Entering into agreements for selling concessions, discounts, commissions, or allowances as consideration for services in connection with the distribution or sale of a security in Hawaii to any non-licensed dealer or salesperson, unless the person is not required to be registered in order to engage in the securities business in this State;
- (13) Operating a securities business while being unable to meet current liabilities, or violating any rule or order relating to minimum capital, bond, record-keeping and reporting requirements, or

provision concerning use, commingling, or hypothecation of customers' funds or securities; or

- (14) Failure or refusal to furnish a customer, upon reasonable request, information to which the customer is entitled, or to respond to a formal written demand or complaint.

(c) Without in any way limiting the generality thereof, for the purposes of section 485-15(4), HRS, any of the following shall demonstrate an applicant's or registrant's unworthiness to transact the business of an investment adviser or investment adviser representative:

- (1) Causing unreasonable delay or failure to execute orders, liquidate customers' accounts, or in making delivery of securities purchased or remittances (or credit) for securities sold;
- (2) Selling securities at unfair prices in relation to market value, or with unreasonable or excessive markups or commissions;
- (3) Effecting transactions in the account of a customer without the customer's knowledge or consent or maintaining discretionary accounts without written authorization;
- (4) Placing an order upon instruction from a third party without client authorization;
- (5) Wilful switching, churning, overtrading, or reloading of securities in a customer's account for the ostensible purpose of accumulating or compounding commissions;
- (6) Inducing a customer to invest beyond the customer's known immediate financial resources, or without regard to the nature and character of the account;
- (7) Recommending any security when the investment adviser knew or should have known that the issuer would not conduct business or fulfill its representations;
- (8) Borrowing or lending money or securities except when the investment adviser is a registered broker-dealer providing margin accounts;
- (9) Representing oneself as a financial planner, consultant, or adviser without accurately describing services, qualifications, and method of compensation;
- (10) Placing an order for a security which the investment adviser should have known is not registered or exempt from registration;
- (11) Placing an order through an unlicensed broker or agent which the investment adviser should have known was unlicensed;
- (12) Providing a report or recommendation to a client prepared by someone other than the investment adviser without disclosing that fact; provided this shall not apply to published research or

- statistical reports, or where an investment adviser orders reports in the normal course of business;
- (13) Engaging or aiding in "boiler room" operations or high-pressure tactics in connection with the promotion of speculative offerings or "hot-issues" by means of an intensive telephone campaign or unsolicited calls to persons not known by, nor having an account with the investment adviser represented by the applicant, whereby the prospective purchaser is encouraged to make a hasty decision to buy, irrespective of the prospective purchaser's investment needs and objectives;
 - (14) Participating in the solicitation or offer for sale of promotional securities without the use and dissemination of a prospectus (where required), or making oral or written statements contrary to or inconsistent with the disclosures contained therein;
 - (15) Making false, misleading, deceptive, exaggerated, or flamboyant representations or predictions in the solicitation or sale of a security:
 - (A) That the security shall be resold or repurchased; or
 - (B) That the security shall be listed or traded on an exchange or established market; or
 - (C) That the security shall result in an assured, immediate or extensive increase in value, future market price, or return on investment; or
 - (D) With respect to the issuer's financial condition, anticipated earnings, potential growth, or success; or
 - (E) That there is a guarantee against risk or loss;
 - (16) Failing to disclose a dual agency capacity or effecting transactions upon terms and conditions other than those stated per confirmations;
 - (17) Failing to make a bona fide public offering pursuant to an underwriting agreement or entering into an arrangement which establishes unfair or unreasonable terms and conditions or compensation;
 - (18) Establishing fictitious accounts in order to execute transactions which would otherwise be prohibited;
 - (19) Entering into agreements for selling concessions, discounts, commissions, or allowances as consideration for services in connection with the distribution or sale of a security in Hawaii to any non-licensed dealer or salesperson, unless the person is not required to be registered in order to engage in the securities business in this State;

- (20) Violating any of the provisions of section 16-38-35 that prescribe limitations on advertisements;
- (21) Disclosing the identity, affairs, or investment of any client unless required to do so or unless consented by client;
- (22) Failing to properly supervise the activities of employees to ensure compliance with the law and rules; failing to properly investigate the character, business repute, experience, and qualifications of employees;
- (23) Misrepresenting any advisory client, or prospective advisory client, the qualifications of the investment adviser or any employee of the investment adviser, or misrepresenting the nature of the advisory services being offered or fees to be charged for such service, or to omit to state a material fact necessary to make the statements made regarding qualifications, services, or fees, in light of the circumstances under which they are made, not misleading;
- (24) Charging a client an unreasonable advisory fee;
- (25) Failing to disclose to clients in writing before any advice is rendered any material conflict of interest relating to the adviser or any of its employees which could reasonably be expected to impair the rendering of unbiased and objective advice including:
 - (A) Compensation arrangements connected with advisory services to clients which are in addition to compensation from such clients for such services; and
 - (B) Charging a client an advisory fee for rendering advice when a commission for executing securities transactions pursuant to such advice will be received by the adviser or its employees;
- (26) Guaranteeing a client that a specific result will be achieved (gain or no loss) with advice which will be rendered; or
- (27) Entering into, extending or renewing any investment advisory contract unless such contract is in writing and discloses, in substance, the services to be provided, the term of the contract, the advisory fee, the formula for computing the fee, the amount of prepaid fee to be returned in the event of contract termination or nonperformance, whether the contract grants discretionary power to the adviser and that no assignment of such contract shall be made by the investment adviser without the consent of the other party to the contract. [Eff 6/4/70; am and ren §16-38-7, 7/30/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-15)

SUBCHAPTER 5

REGISTRATION OF SECURITIES, PROSPECTUS

§16-38-8 Registration of securities. (a) Application to register securities for distribution in the State of Hawaii may be filed with the commissioner in substantially the form and content required by the application form together with exhibits required for the registration by notification, coordination, and qualification, as the case may be. An application for the registration of securities by notification shall be prepared, meeting the requirements of section 485-9(b), HRS. The U-1 form shall be accepted for filing by notification, coordination, and qualification.

(b) A registration statement relating to a security issued by a face amount certificate company or a redeemable security issued by an open-end management company or unit investment trust shall be by coordination.

(c) An application filed with the SEC under the Securities Act of 1933, Regulation A, 17 CFR Rules 230.251 to 230.262 may be filed with the commissioner either by notification or qualification, but not by coordination. Notwithstanding the requirements of the SEC, however, the prospectus or offering circular used in connection with an offering of securities under regulation A of the SEC shall contain the financial statements prescribed by section 485-9, HRS, (notification) or section 485-10, HRS, (qualification). [Eff 6/4/70; am and ren §16-38-8, 7/30/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-9, 485-10)

§16-38-9 Prospectus. (a) The prospectus may be printed, mimeographed, lithographed, or typewritten, or prepared by any similar process in clearly legible copies. If printed, it shall be set in roman type of at least ten-point, modern type, (except that financial statements and other statistical or tabular matter may be set in roman type as small as eight-point). All type shall be leaded at least two points.

(b) Every subscription agreement concerning a registration of securities by qualification shall contain a statement by the purchaser that the purchaser has received a copy of the prospectus covered by the registration.

(c) Interstate offerings shall contain the information required by the application form together with the following:

- (1) How the public offering price was established;
- (2) Whether there has been a public market for the securities;
- (3) Terms and conditions of the escrow agreement; and
- (4) Business history of the officers and directors.

(d) Intrastate offerings shall contain the same information as interstate offerings, plus the following:

- (1) That the offering is only to bona fide residents of the State of Hawaii;
 - (2) That during the public offering no securities may be transferred to a non-resident of Hawaii;
 - (3) That in case of a sale to a non-resident, the issuer may rescind the sale and refund the purchase price; and
 - (4) In an offering of interest-bearing securities, what reserves or sinking fund shall be provided to pay for the securities as they become due, or whether no reserves shall be provided.
- (e) The prospectus shall be prepared in substantially the following form and shall contain the information as hereinafter specified together with any additional data as the commissioner may prescribe. (The following specimen form has been prepared for use in connection with a speculative intrastate offering and may therefore be modified to the extent the provisions are inapplicable.)

- (B) Describe the physical properties, equipment, claims, patents, or patent applications, etc., and nature of title or interest therein;
 - (C) If issuer leases its plant, office, or other physical properties, disclose briefly the terms of the lease and relationship of lessor to any officer, director, promoter, or stockholder of the issuer;
 - (D) State the nature of present or proposed products or services, the principal market therefor;
 - (E) Set forth the general competitive conditions in the industry or business in which issuer is, or proposes to be, engaged, and any particular risks or hazards to which it might be subjected; and
 - (F) Describe the issuers employee relations by setting forth number of employees and whether any of them are covered by collective bargaining agreements and, if so, approximately how many are so covered, when agreements expire, and whether collective bargaining is on a company or industry wide basis. Also describe whether the issuer has experienced any work stoppages in recent years;
- (3) Use of proceeds. Outline the proposed plans, objectives, or programs of the issuer and make a reasonable itemized statement of the purposes for which the net proceeds to the issuer from the sale of securities are to be used and the amounts to be used for each purpose, indicating the order of priority;
- (4) Method of offering. If the securities are to be offered through a dealer, state the name and address of the dealer, with a statement of any material relationship between the issuer and the dealer. State whether the securities are to be offered for cash only or whether the securities may be paid for in installments and, if so, the terms and conditions. If a minimum purchase is required, it should also be disclosed. State briefly the commission to be paid to the dealer, including cash, securities, contracts, options, or any other consideration. If the securities are to be sold by the issuer, it should also be stated that the offering shall be done by securities salespersons duly registered with the commissioner of securities. If the proceeds of the offering are to be placed in escrow, state the terms and conditions of the escrow, which shall provide among other terms as the commissioner may prescribe for the certification by the escrow agent to the commissioner when the amount specified in the escrow agreement has been met in the specified

time and the conditions whereby the funds shall be released to the subscribers by the escrow agent. State also that during the public offering no securities may be transferred to a non-resident and that in case of a sale to a non-resident, the issuer shall rescind the sale and refund the purchase price;

- (5) Speculative features of the offering. Explain generally the speculative features of the offering and any special conditions which may affect the success or failure of the enterprise or the investor's interest therein. State how the public offering price was established and whether there has been a public market for the shares. In a speculative offering, the front cover shall contain a statement that the securities are speculative. If the officers, directors, or promoters are receiving or have received salaries, fees, or other compensation from the issuer, indicate the amounts, how paid, and services rendered. (See section 16-38-11.5);
- (6) Description of securities. Outline briefly as follows:
 - (A) In the case of shares, the par or stated value, if any; the rate of dividend, if fixed, whether cumulative or noncumulative and any restrictions on dividend payments; the preference, if any; and if convertible, the conversion rate; the restrictions, if any, on the transfer of the securities;
 - (B) In the case of debt securities, the rate of interest; the date of maturity or, if the issue matures serially, a brief indication of the serial maturities; if the issue is redeemable before maturity, a brief statement of the redemption date or dates and price or prices; if payment of principal or interest is contingent, an indication of the contingency; a brief indication of the priority of the issue; and if convertible, the conversion rate; and
 - (C) In the case of any other kind of security, appropriate information of a comparable character.
- (7) Management and control. List the names and residence addresses of all officers and directors of the issuer and of any person or persons controlling the issuer and, if the issuer was organized within the last three years, the names and addresses of all promoters of the issuer. For each person listed, show the business history;
- (8) Interests with management. Make a description of all direct or indirect interests, by security holdings or otherwise, of each officer and director of the issuer and, if the issuer was organized within the last three years, of each promoter of the issuer:

- (A) In the issuer or its affiliates; and
 - (B) In any material transactions within the past two years or in any material proposed transactions to which the issuer or any of its predecessors or affiliates was or is to be a party, stating the cost to those persons of any property or services for which payment by or for the account of the issuer has been or is to be made;
- (9) Ownership. If the issuer was organized within the last three years, a statement of the percentage of outstanding securities of the issuer which shall be held by directors, officers, and promoters as a group, and the percentage thereof which shall be held by the public if all of the securities to be offered are sold, and the respective amounts of cash (including cash expended for property transferred to the issuer) paid therefor by the group and by the public;
 - (10) Options and warrants. A brief description of all options or warrants presently outstanding or proposed to be granted to purchase securities of the issuer, including the names of the holders thereof, the cost thereof to the holders, the terms and conditions on which they may be exercised, and the price at which the securities may be acquired pursuant thereto;
 - (11) Litigation. Briefly describe any material pending legal proceedings other than ordinary routine litigation incidental to the business to which the issuer or any of its subsidiaries is a party or of which any of their property is the subject;
 - (12) Legal opinion. State the name and address of the attorney who has advised the issuer with respect to the legality and validity of the securities and their issuance;
 - (13) Escrow provisions. If the officers, directors, promoters, or insiders have stock which is subject to escrow pursuant to section 485-18 of the Hawaii securities act or subject to escrow pursuant to any state or federal statute or regulation, make a complete disclosure of the number of shares escrowed, name of persons escrowing the stock, where escrowed, and the terms and conditions of the escrow; and
 - (14) Financial statements. A balance sheet of the issuer at the close of the issuer's last fiscal year preceding the date of filing of the prospectus, and a profit and loss statement and analysis of surplus for the fiscal year ended at the date of the balance sheet, all certified by an independent public accountant, together with a balance sheet of the issuer as of a date within ninety days prior to the date of filing of the prospectus and a statement of profit and

loss for the period from the close of the last preceding fiscal year to the date of the balance sheet, both verified by a duly authorized officer of the issuer or, if the issuer has been in existence for less than one year, a balance sheet of the issuer as of a date within ninety days prior to the date of filing and a statement of profit and loss for the period from the date of the issuer's organization to the date of the balance sheet, both certified by an independent public accountant.

If consolidated financial statements are used, there should also be a financial statement of the issuer alone. If the issuer has not yet commenced business, there should be submitted in lieu of the statement of profit and loss a statement of receipts and disbursements certified to by an independent public accountant. [Eff 6/4/70; am and ren §16-38-9, 7/30/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-9, 485-10, 485-18)

§16-38-10 Residential cooperative corporations. The information required shall be as prescribed in the application form together with other information as the commissioner may prescribe. [Eff 6/4/70; am and ren §16-38-10, 7/30/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-7)

SUBCHAPTER 6

STATEMENTS OF POLICY RELATING TO REGISTRATION OF SECURITIES

§16-38-11 Registration of securities by qualification. The commissioner shall look with disfavor and reject any application for registration of securities as being fraudulent or working or tending to work a fraud upon the purchaser, or may find that the enterprise or business of the issuer is based on unsound business principles, unless the following requirements are met or good cause is shown for an exception. [Eff 6/4/70; am 8/8/71; am and ren §16-38-11, 7/30/81; am and comp 10/12/85; comp] (Auth: HRS §485-2) (Imp: HRS §§5-2, 485-10, 485-18)

§16-38-11.1 Financial reports. Financial statements as required hereunder shall be prepared, audited, and certified by independent certified public accountants or licensed independent public accountants in accordance with generally accepted accounting procedures and practices, applied on a consistent

basis. If a report contains exceptions of a material nature, it shall not be considered to be certified. [Eff 6/4/70; am 8/8/71; am and ren §16-38-11, 7/30/81; am, ren §16-38-11.1 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-2, 485-10, 485-18)

§16-38-11.2 Maximum commissions and expenses. Compensation to dealers in connection with the sale and promotion of a public offering, including selling expenses and allowances or reimbursement for items as salaries, overrides, salesperson's commissions, clerical, administrative, printing, postage, advertising, and all other expenditures incurred, and anything of value accruing to the dealer directly or indirectly, shall not exceed fifteen per cent of the total amount of the offering. [Eff 6/4/70; am 8/8/71; am and ren §16-38-11, 7/30/81; am, ren §16-38-11.2 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-2, 485-10, 485-18)

§16-38-11.3 Promotional securities. (a) If an issuer:

- (1) Is in the promotional, exploratory, or development stage; or
- (2) Has been organized within three years prior to the date of filing the application for registration of securities; or
- (3) Has issued any equity securities of or substantially of the same class as those sought to be registered to promoters, officers, directors, or underwriters of the issuer within three years prior to the date of filing, or is or proposes to become committed to issue any equity securities of or substantially of the same class as those sought to be registered to any promoter, officer, director, or underwriter of the issuer, in any case at a price less than the public offering price of the securities sought to be registered; or
- (4) Has issued any equity securities of or substantially of the same class as those sought to be registered within three years prior to the date of filing for a consideration other than cash;

then conditions and restrictions in subsection (b) shall apply unless good cause shall be shown for the waiver of one or more or all of the conditions and restrictions.

(b) The following restrictions shall apply to any issuer who is subject to subsection (a):

- (1) The purchase price paid or payable for any securities referred to in subsection (a)(3) or (4) shall be not less than twenty-five per cent of the public offering price of the securities to be registered;

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- (2) Each promoter, officer, director, and underwriter who shall have acquired or to whom it is proposed to issue any security, or right or option to acquire a security, referred to in subsection (a)(3) or (4), shall file with the issuer and the commissioner a written representation that the security has been or upon the exercise of any right or option shall be acquired for investment and not for distribution, and that no security shall be transferred (other than by operation of law or by will or the laws of descent) for a period of one year after termination of the public distribution;
- (3) The book value (determined in accordance with generally accepted accounting principles disregarding any operating losses incurred after the date of filing of the application for registration) of the equity securities outstanding upon completion of the public offering (assuming all securities so offered to be sold) shall be not less than two-thirds of the public offering price; and
- (4) Shares issued for a consideration other than cash shall be required to be held in escrow pursuant to section 485-18, HRS, and a summary of the escrow provisions shall be required to be included in the prospectus. [Eff 6/4/70; am 8/8/71; am and ren §16-38-11, 7/30/81; am, ren §16-38-11.3 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-2, 485-10, 485-18)

§16-38-11.4 Options and warrants. Options and warrants and other acquisitions or conversion rights granted to or reserved for officers, directors, promoters, or insiders shall be fully justified, reasonable in number and method of exercise, and meet the following requirements:

- (1) A complete explanation for the basis and reason for the issuance shall be provided;
- (2) The total number of underlying shares subject to options does not exceed ten per cent of the shares to be outstanding if all shares being offered are sold;
- (3) The rights are not exercisable during the effectiveness of the public offering nor for a period of eleven months from date issued, and the exercise price thereafter of not less than the percentage amounts provided in the following schedule:

Period at which exercise privilege may take place	Per cent of public offering price at which rights may be exercised
After 1 year from issuance	107%
2 years from issuance	114%
3 years from issuance	121%
4 years from issuance	128%

- (4) The rights are not exercisable after the expiration of five years from date of issue; and
- (5) Options or warrants to dealers or underwriters do not exceed the limitations imposed by section 16-38-11.2 relating to maximum commissions allowable as compensation in whole or in part for the sale of securities and shall be nontransferable. Options or warrants issued to all shareholders pro rata, or in connection with qualified stock options to employees which meet the requirements of the United States Internal Revenue Code, or other employees' options pursuant to a stock purchase or profit-sharing plan, shall not be subject to the restrictions provided in this section if they are justified and reasonable in number and method of exercise. [Eff 6/4/70; am 8/8/71; am and ren §16-38-11, 7/30/81; am, ren §16-38-11.4 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-2, 485-10, 485-18)

§16-38-11.5 Impoundment of proceeds. (a) The commissioner shall ordinarily require, as a condition to registration of speculative and promotional securities, that all proceeds from the sale of securities less selling expenses be impounded in escrow until the time that a sufficient amount has been realized to accomplish the purposes of the offering. Speculative and promotional securities shall be defined as securities issued by a company that is organized within three years of the filing, that has no earnings record, is in the development, exploratory or promotional stage, and is financing an initial or proposed enterprise, or is a company in poor financial condition intending to raise additional working capital to continue its operation. An executed copy of the escrow agreement shall be filed with the commissioner and shall contain the following information in addition to whatever other information the commissioner may require:

- (1) Funds required to be impounded shall be deposited in a separate trust account with a bank, a corporate trustee, or similar institution authorized to do business in this State, or other person acceptable to the commissioner;
 - (2) Net proceeds to be returned directly to the investors by the escrow holder and not through the intermediary of the issuer in the event that the minimum prescribed amount is not obtained within the specified period, in the event the depositor shall certify to the commissioner that the terms and conditions of the escrow agreement have not been met and request authorization to return the impounded funds to the purchasers. If the minimum prescribed amount is obtained within the specified period, the depositary shall so certify to the commissioner and request authorization to release the impounded funds to the issuer;
 - (3) No certificates evidencing securities purchased (other than subscription agreements or receipts) shall be issued until after release of the funds from escrow;
 - (4) In the event that checks, drafts, money orders or other remittances are not made payable to the depositary, all monies received from the sale of securities, after collection, and deduction for allowable selling commission and expenses, the issuer, or dealer, if any, shall promptly (and in no event later than ten days after receipt thereof) transmit to the depositary the net amount required to be impounded;
 - (5) A commitment by the depositary to furnish to the commissioner or his staff, upon request for information, data concerning the status of, or amounts on deposit in, the escrow account;
 - (6) Ordinary and standard terms and conditions which are generally required by escrow agents in connection with payment of fees, charges and expenses, liability, claims, litigation, notice and hold-harmless and indemnification clauses, etc.; and
 - (7) That no funds are to be released from impoundment, and no changes effectuated in the agreement except by written consent and authorization of the commissioner.
- (b) A request for a modification of the escrow arrangements as accepted, or for partial release of the funds so impounded, shall be generally regarded with disfavor, and shall be granted only upon good cause shown, and by application containing the following information:
- (1) A certified statement from the depositary setting forth the total amount of subscriptions and the character of each deposit; and

- (2) A waiver and consent executed by each purchaser or subscriber whose funds are sought to be released, or, an acknowledgment by the purchaser or subscriber that an offer for return of investment has been made and rejected. The offer, or solicitation for waiver and consent shall recite:
 - (A) That the issuer has failed to meet the impoundment conditions required, if that is the case;
 - (B) The asserted reasons for requesting a partial release of funds or modification of the escrow arrangements; and
 - (C) A statement that the subscriber realizes that the subscriber is under no obligation to give consent and waiver, and that the consent and waiver is freely and voluntarily given. [Eff 6/4/70; am 8/8/71; am and ren §16-38-11, 7/30/81; am, ren §16-38-11.5 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-2, 485-10, 485-18)

§16-38-11.6 Limit of debt securities-interstate offerings. The total amount of unsecured interest-bearing securities, excluding investment certificates, that may be registered or may be outstanding at any time shall not exceed five times the net worth of the issuer, provided that, if the issuer maintains reserves to pay for securities as they become due, the reserves may be included in determining the ratio. [Eff 6/4/70; am 8/8/71; am and ren §16-38-11, 7/30/81; am, ren §16-38-11.6 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-2, 485-10, 485-18)

§16-38-11.7 Real estate investment trusts. (a) Applications to register securities issued or issuable by a real estate investment trust shall substantially meet the requirements of this section.

(b) A real estate investment trust is defined as an unincorporated trust or association which intends to comply with sections 856, 857, and 858 of the Internal Revenue Code of 1954, as amended.

(c) The declaration of trust, or other instrument forming the trust, among other things, shall ordinarily contain provisions as set forth in subsections (d) to (1).

(d) A majority of the trustees shall not be affiliated with the adviser of the trust or any organization affiliated with the adviser of the trust. The trustees shall be elected by the shareholders of the trust annually.

(e) No trustee, officer, or adviser of a trust, or any person affiliated with any trustee, officer, or adviser of a trust, shall sell any property or assets to

the trust or purchase any property or assets from the trust, directly or indirectly, nor shall any trustee, officer, or adviser of a trust receive any commission or other remuneration, directly or indirectly, in connection with the purchase or sale of trust assets, except pursuant to transactions that are fair and reasonable to the shareholders of the trust and that relate to:

- (1) The acquisition of property or assets at the formation of the trust or shortly thereafter that is fully disclosed in the prospectus;
- (2) The acquisition by the trust of federally insured or guaranteed mortgages at prices not exceeding the currently quoted prices at which the Federal National Mortgage Association is purchasing comparable mortgages;
- (3) The acquisition of other mortgages on terms not less favorable to the trust than similar transactions involving unaffiliated parties; or
- (4) The acquisition by the trust of other property at prices not exceeding the fair value thereof as determined by independent appraisal.

All transactions and all other transactions in which any persons have any direct or indirect interest shall be approved by a majority of the trustees, including a majority of the independent trustees. All commissions or remuneration received by any trustee, officer, or adviser of a trust in connection with any transactions shall be deducted from the advisory fee.

(f) The aggregate annual expenses of every character paid or incurred by the trust, excluding interest, taxes, expenses in connection with the issuance of securities, shareholder relations, and acquisition, operation, maintenance, protection, and disposition of trust properties, but including advisory fees and mortgage servicing fees and all other expenses, shall not exceed the greater of:

- (1) One and one-half per cent of the average net assets of the trust, net assets being defined as total invested assets at cost before deducting depreciation reserves, less total liabilities, calculated at least quarterly on a basis consistently applied; or
- (2) Twenty-five per cent of the net income of the trust, excluding provision for depreciation and realized capital gains and losses and extraordinary items, and before deducting advisory and servicing fees and expenses, calculated at least quarterly on a basis consistently applied; but in no event shall aggregate annual expenses exceed one and one-half per cent of the total invested assets of the trust.

The adviser shall reimburse the trust at least annually for the amount by which aggregate annual expenses paid or incurred by the trust as defined herein exceed the amounts herein provided.

(g) The aggregate borrowings of the trust, secured and unsecured, shall not be unreasonable in relation to the net assets of the trust, as defined in subsection (f) and the maximum amount of borrowings in relation to the net assets shall be stated in the prospectus.

(h) A real estate investment trust shall ordinarily have a net capital of not less than \$100,000 represented by outstanding shares or certificates of beneficial interest.

(i) A trust shall not:

- (1) Engage in any material trading activities with respect to its properties;
- (2) Issue redeemable equity securities or equity securities of more than one class;
- (3) Issue debt securities to the public unless the historical cash flow of the trust or the substantiated future cash flow of the trust, excluding extraordinary items, is sufficient to cover the interest on the debt securities; or
- (4) Issue options or warrants to purchase its securities to the adviser of the trust or any person affiliated with the adviser, or to any other persons at exercise prices less than the fair market value of the securities on the date of grant.

(j) Any advisory contract entered into by the trust prior to the initial public offering shall be for a period not longer than three years, and any contract entered into thereafter shall be for a period not longer than one year. Any advisory contract shall provide that it may be terminated at any time without penalty, by the trustees or a majority of the holders of outstanding shares of beneficial interest, upon not less than sixty days' written notice to the adviser.

(k) The trust shall prepare an annual report concerning its operations for each fiscal year ending after the public offering of its securities, including financial statements prepared in accordance with generally accepted accounting principles applied on a consistent basis and certified by independent public accountants. The annual report shall be delivered to each public shareholder and debenture holder within one hundred twenty days after the end of the fiscal year. There shall be an annual meeting of the holders of outstanding shares of beneficial interest of the trust, upon reasonable notice, following delivery of the annual report.

(l) The investment policies intended to be followed by the trustees should be stated with reasonable particularity and shall contain express statements of policy with respect to unimproved real estate and junior mortgages, including the risks inherent with the policies. [Eff 6/4/70; am 8/8/71; am and ren §16-38-11, 7/30/81; am, ren §16-38-11.7 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-2, 485-10, 485-18)

§16-38-11.8

§16-38-11.8 Offering price. In the case of an issuer which has been actually engaged in business or operation, the amount for which a security is being offered to the public should bear some reasonable relationship to:

- (1) Market value, if any; or
- (2) Price-earnings ratio, as reflected by its financial statements covering an average three-year preceding period, or the shorter duration of experience or operation as may be applied; or
- (3) In the absence of an established or determinable market value or price-earnings ratio, the book value of the issuer may be taken into consideration in justifying or substantiating the reasonableness of the offering price. [Eff 6/4/70; am 8/8/71; am and ren §16-38-11, 7/30/81; am, ren §16-38-11.8 and comp 10/12/85; comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-2, 485-10, 485-18)

§16-38-11.9 Compliance with Hawaii general corporation law. No application of a Hawaii corporation for the registration of securities shall be accepted if the corporation is not current in filing its annual corporation exhibits as required by the general corporation law, and complete records as prescribed by the general corporation law shall at all times be maintained. [Eff 6/4/70; am 8/8/71; am and ren §16-38-11, 7/30/81; am, ren §16-38-11.9 and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§416, 485-2, 485-10, 485-18)

§16-38-12 REPEALED. [R 10/12/85]

SUBCHAPTER 7

EFFECTIVENESS AND POST-EFFECTIVENESS REQUIREMENTS

§16-38-13 Effectiveness. When an application for the registration of securities has been accepted and declared effective by the commissioner, it shall be designated as a registration statement, and the offering may be commenced upon the issuance of a certificate of registration or notification of effectiveness. A registration statement that has become effective with the SEC under the Securities Act of 1933, 15 U.S.C. 77a, becomes effective in Hawaii automatically at the moment of effectiveness with the SEC if no stop order or notice of deficiency has been entered. The applicant shall promptly advise the commissioner by telephone or telegraph of the date and time of federal

effectiveness. [Eff 6/4/70; am and ren §16-38-13, 7/30/81; comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-15)

§16-38-14 Confirmations by issuer. Every issuer selling its own securities in an intrastate offering, at or before completion of a transaction, shall give or send to each customer written confirmation, retaining copies thereof, concerning all sales of securities, and disclosing:

- (1) Date the transaction occurred;
- (2) Price and commission charged; and
- (3) Name of salesperson handling the transaction. [Eff 6/4/70; am and ren §16-38-14, 7/30/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-2)

§16-38-15 Amendments. If prior to or during the period of effectiveness any statement, document, or information contained in the registration statement or prospectus becomes materially inaccurate, incorrect, or misleading, or in the light of changes in circumstances, addendums are made necessary in order to present a full disclosure of material facts affecting the issuer's business or the offering, or if the commissioner requests additional data, information, or verification thereof, the registrant shall promptly file, and in no event later than fifteen days following the event, occurrence, discovery, or notice thereof necessitating same, a correcting amendment. A registration statement relating to a security issued by a face amount certificate company or a redeemable security issued by an open-end management company or unit investment trust, as those terms are defined in the Investment Company Act of 1940, 15 U.S.C. 80a, may be amended after its effective date so as to increase the securities specified therein as proposed to be offered. Upon approval of the amendment by the commissioner, the revised date together with the date of the prospectus shall be shown on the front cover, and the portion or portions of the prospectus being amended should also show the amended date. [Eff 6/4/70; am and ren §16-38-15, 7/30/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-10)

§16-38-16 Renewals. The registration statement may be renewed not less than fifteen days prior to the expiration date by filing a new prospectus containing information of a date not more than ninety days prior to the date of filing, together with the renewal fee of \$20. The front cover shall show the balance of the offering, the amount of the original registration, and the date the original

registration became effective. [Eff 6/4/70; am and ren §16-38-16, 7/30/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-10, 485-11)

§16-38-17 Withdrawal, termination, or completion. (a) Request for withdrawal of a registration may be made before or after effectiveness by written notification. However, no request shall be granted during the pending of a stop order proceeding under section 485-13, HRS, unless the commissioner finds that the stop order is not necessary in the public interest. Upon the granting of a request for withdrawal, no part of the registration fee shall be refunded.

(b) Notification of termination or completion of an offering shall be submitted to the commissioner within thirty days after the termination or completion, and shall include the results of the offering. [Eff 6/4/70; am and ren §16-38-17, 7/30/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-9, 485-10, 485-11, 485-13)

SUBCHAPTER 8

ADVERTISING AND FINANCIAL REPORTS

§16-38-18 Advertising. Any written advertising or subscription, recording, radio and television announcements, broadcast or commercial to be used in connection with the sale of securities in Hawaii, except securities exempt under section 485-4, HRS, (exempt securities) and section 485-6, HRS, (exempt transactions) and "tombstone" advertisements placed in newspapers or periodicals shall be filed with the commissioner at least two days prior to its proposed use. However, all advertising material previously filed with and cleared by the SEC or NASD is exempt from filing. [Eff 6/4/70; am 5/27/80; am and ren §16-38-18, 7/30/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-25)

§16-38-19 Reports. A copy of all financial reports to be sent to security holders while a registration statement is in effect shall be filed with the commissioner. [Eff 6/4/70; am and ren §16-38-19, 7/30/81; comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-16)

SUBCHAPTER 9

BOND

§16-38-20 Cancellation of bond. The surety of any bond issued under chapter 485, HRS, or this chapter may cancel the bond by giving sixty days' notice in writing to the commissioner, and shall thereafter be relieved of any liability for any breach of condition occurring after the effective date of cancellation. [Eff 5/27/80; am and ren §16-38-20, 7/30/81; am and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-2)

SUBCHAPTER 10

EXEMPT TRANSACTIONS

§16-38-21 Limitation on issuers and offerors. (a) Nothing in this subchapter shall relieve, or be construed as in any way relieving, issuers or persons acting on their behalf from providing disclosure to prospective investors adequate to satisfy the anti-fraud provisions of chapter 485, HRS.

(b) In viewing of the objective of this subchapter and the purpose and policies underlying chapter 485, HRS, these exemptions are not available to any issuer or persons acting on their behalf with respect to any transaction which, although in technical compliance with this subchapter, is part of a plan or scheme to evade registration or the conditions or limitations explicitly stated in this subchapter.

(c) Nothing in this subchapter is intended to exempt registered broker-dealers or agents from the due diligence standards otherwise applicable to registered persons.

(d) Nothing in this subchapter is intended to exempt any person from the broker-dealer or agent requirements from chapter 485, HRS. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-6)

§16-38-22 Exemptions. (a) Any offer or sale of securities offered or sold in compliance with the Securities Act of 1933, Regulation D, 17 CFR, Rules 230.501, 230.502, 230.503, 230.505, and 230.506 as made effective in Release No. 33-6389 and complies with the conditions and limitations of this subchapter, shall be exempted under section 485-6(15), HRS.

(b) This section shall not apply to any offer or sale of securities offered or sold in compliance with the Securities Act of 1933, Regulation D,

Rule 230.504, made effective in Release No. 33-6389. [Eff and comp 10/12/85]
(Auth: HRS §485-2) (Imp: HRS §485-6)

§16-38-23 Filing. (a) The issuer shall file with the commissioner a signed copy of Form D (17 CFR §239.500) and State registration form, not later than ten days after the first offer is made in the State.

(b) An executed consent to service of process and corporate resolution, if issuer is a corporation, shall be included unless a currently effective consent to service of process is on file with the commissioner.

(c) Upon written request of the commissioner, the issuer shall provide information furnished by the issuer to the offerees. [Eff and comp 10/12/85]
(Auth: HRS §485-2) (Imp: HRS §485-6)

§16-38-24 Disqualification. (a) Any person who is disqualified from using any provision of Regulation D, 17 CFR 230, of the Securities Act of 1933 by the SEC may not qualify for exemptions under this subchapter.

(b) No exemption under this subchapter shall be used if any person or parties of interest described in Securities Act of 1933, Regulation A, 17 CFR 230, Rule 230.252, 17 CFR 230, sections (c), (d), (e), or (f):

- (1) Has filed a registration statement which is the subject of a currently effective stop order entered by any state within five years prior to the commencement of the offering;
- (2) Has been convicted within five years prior to the commencement of the offering of any felony or misdemeanor in connection with an offer or sale of any security;
- (3) Has been convicted within five years prior to the commencement of the offering of any felony or misdemeanor involving fraud or deceit, including but not limited to forgery, embezzlement, obtaining money under false pretenses, larceny, or conspiracy to defraud;
- (4) Is currently subject to any state's administrative order or judgment which prohibits the use of any exemption from registration in connection with the purchase or sale of securities;
- (5) Is currently subject to any state's administrative order or judgment entered by that state's security administrator or commissioner within five years prior to the commencement of the offering or is subject to any state's administrative order or judgment in which fraud or deceit, including but not limited to making untrue statements of material facts or omitting to state material facts was

found and the order or judgment was entered within five years prior to the commencement of the offering; or

- (6) Is currently subject to any order, judgment, or decree of any court of competent jurisdiction temporarily or preliminarily restraining or enjoining, or is subject to any order, judgment, or decree of any court of competent jurisdiction, entered within five years prior to the commencement of the offering, permanently restraining or enjoining the person from engaging in or continuing any conduct or practice in connection with the offer or sale of any security or involving the making of any false filing with any state.

Paragraphs (1), (2), (3), (5), and (6) shall not apply if the person or party subject to the disqualifying order, judgment, or decree is duly licensed or registered to conduct securities related business in the state in which the order, judgment, or decree was entered against the person or party.

(c) Any disqualification caused by this section shall be automatically waived if the federal or state agency which created the basis for disqualification determines upon a showing of good cause that it is not necessary under the circumstances that the exemptions be denied. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-6)

§16-38-25 Advertising. Neither the issuer nor any person or party acting on behalf of the issuer shall offer or sell the securities by any form of general solicitation or general advertising, directly or indirectly, including but not limited to the following:

- (1) Any advertisement, article, notice, or other communication published in any newspaper, magazine, or similar media or broadcast over radio, television, or cable television system; and
- (2) Any seminar or meeting whose attendees are invited by any general solicitation or general advertising. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-6)

§16-38-26 Integration. A separate sale of securities within or without this State shall be included as part of the same offering if, after considering the following elements, the particular facts and circumstances indicate the sale to be part of the same offering. The elements to be considered are whether the:

- (1) Sales are part of a single plan of financing;
- (2) Sales involve issuance of the same class of security;
- (3) Sales are made at or about the same time;
- (4) Same type of consideration is received; and

- (5) Sales are made for the same general purpose. [Eff and comp 10/12/85; comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-6)

§16-38-27 Limitation on expenses. All expenses of the issues with regard to the securities registered under this subchapter, including but not limited to expenses relating to sales, management fees, acquisition of real or personal property, entertainment, commissions, salaries, and cost of preparation of the offer, shall be reasonable considering the proposed use of the funds raised, the amount to be raised, the type of security being issued, and the relative risk of the investment. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-6)

§16-38-28 Escrow of funds raised. (a) An escrow shall be established where, because of the nature of the intended use of the funds, nature of the project or business plan, a minimum amount of funds shall be raised in order that the project can get underway with a reasonable chance of success even if no further sales are made.

- (b) The requirements for an escrow under this section are:

- (1) The escrow agent shall be a licensed escrow depository under chapter 449, HRS, or an excepted institution under section 449-3, HRS; and
- (2) The escrow terms shall include instructions that the funds placed into escrow shall be held in trust for the benefit of the investors and shall not be released to the issuer until the minimum amount of funds set forth in the registration has been raised.

(c) The requirements of this section may be waived by the commissioner upon a showing that the escrow is not necessary and that the investor is adequately protected. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-6)

§16-38-29 Fees. The filing fee for any exemption granted under this subchapter shall be \$100, all of which shall be deposited into the compliance resolution fund. [Eff and comp 10/12/85] (Auth: HRS §§485-2, 26-9) (Imp: HRS §485-6)

SUBCHAPTER 11

INVESTMENT ADVISERS

§16-38-33 Registration; generally. (a) A person, corporation, partnership, or other unincorporated association may be registered as an investment adviser under chapter 485, HRS, if the commissioner finds that the applicant is of good repute and otherwise satisfies the requirements of chapter 485, HRS, and this chapter.

(b) All investment advisory services shall be made pursuant to a written investment advisory contract and shall be subject to disclosure requirements specified in section 16-38-38. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-34 Registration; eligibility requirements. (a) An applicant, if a natural person, shall have attained the age of eighteen years;

(b) A partner, officer, representative, or employee of a registered investment adviser may render investment advisory services only if the person meets all the requirements of and has been duly registered as an investment adviser, as provided by section 485-14, HRS.

(c) A corporation, partnership, sole proprietorship, or other unincorporated association whose partners, officers, representatives, or employees render investment advisory services as defined in section 485-1(6), HRS, shall comply with registration procedures as provided by section 485-14, HRS, and this chapter, unless otherwise exempted.

(d) An applicant shall have a minimum net worth, as defined in section 16-38-36, of not less than \$5,000, if the applicant has custody or discretionary authority over client funds.

(e) An applicant shall obtain insurance covering the adviser's business for errors and omissions for at least \$100,000 per occurrence, with a \$200,000 aggregate for advisers with less than two years' experience or coverage for \$100,000 per occurrence with a \$500,000 aggregate for advisers with two or more years of experience. An investment adviser who commences a second year of experience during the interim period between registration and renewal shall submit within thirty days after the commencement of the second year proof of the higher insurance coverage commensurate with the above mentioned amounts.

(f) In the case of a foreign corporation or a partnership intending to establish a branch in Hawaii, compliance shall be made with the requirements of the Hawaii foreign corporation law (chapter 418, HRS) or the Hawaii partnership

law (chapter 425, HRS), respectively. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-35 Registration; application. (a) An application for original or renewal registration shall be filed on a form prescribed by the commissioner or, in the case of an original application, on a form approved by the Securities and Exchange Commission and the State, and shall contain the information requested therein concerning the applicant's identification, qualification, business association, history, repute, experience, and financial condition.

(b) The application shall be filed together with the following:

- (1) A filing fee of \$50;
- (2) Consent to service of process;
- (3) If the applicant is a natural person, the applicant's photograph;
- (4) A copy of a written disclosure statement, as provided by section 485-25(c)(4), HRS, if the adviser engages in activities which are applicable under that section;
- (5) A \$50,000 bond or cash or securities in lieu thereof if the adviser retains custody or possesses discretionary authority over clients' money, securities, or other assets; or a \$5,000 bond or cash or securities in lieu thereof if the adviser does not retain custody or possess such authority;
- (6) A balance sheet as of a date within thirty days of filing, or if applicant has been engaged in business one year or more preceding, a balance sheet certified by an independent public accountant as of the last fiscal year, together with a balance sheet verified by the applicant as of a date within thirty days of filing. However, if the applicant does not have custody or discretionary authority over client funds, the adviser need only file financial statements verified by the adviser;
- (7) A certificate of insurance covering the adviser's business for errors and omissions, as specified by section 16-38-34; and
- (8) Proof that the applicant has passed the exam requirement as provided by section 16-38-37, or otherwise qualifies for exemption from the exam as specified in section 16-38-37. The applicant shall specify the number of times of failure to pass the exam requirement provided by section 16-38-37 or the SEC examination.

(c) Additional exhibits or information not specifically required by the application but essential to a full presentation of all material facts relating to applicant's qualification should be furnished properly identified.

(d) The commissioner may make the examination of the applicant and require additional information deemed appropriate in consideration of the applicant's eligibility for registration.

(e) An applicant for renewal of registration need not furnish the identical information schedules or exhibits submitted in connection with an original application, unless there has been a change in circumstances affecting previous disclosures or the data is specifically requested by the commissioner. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-36 Registration; financial requirements. (a) Every adviser currently registered shall file an annual report of condition within ninety days following the end of the calendar or fiscal year adopted as follows:

- (1) An adviser registered with the SEC shall file a copy of the financial report filed with the SEC; and
- (2) An adviser not registered with the SEC or who is not required to file with the SEC shall file a balance sheet, including analysis of surplus, certified by an independent public accountant in conformance with generally accepted accounting principles. However if an adviser does not have custody or discretionary authority over client funds, the adviser shall file financial statements verified by the adviser. Any statement which does not adequately reflect the applicant's true financial picture shall not be accepted;

(b) Each registered adviser who is required under section 485-14(q) shall have at all times a minimum net worth of not less than \$5,000 which as used herein shall mean net worth, or the difference between total assets and total liabilities or indebtedness, after adjustment to eliminate or revise assets of doubtful or uncertain value and to reflect true liabilities, in accordance with the following schedule of asset items to be adjusted or substantiated:

- (1) Securities owned shall be adjusted to market value;
- (2) Value of real estate shall be attested to by qualified and disinterested persons;
- (3) Property in joint ownership shall be limited to applicant's interest therein; and
- (4) Value of unsecured notes, accounts receivable, or advanced commissions due from a salesperson, officer, director, partner, or affiliate may be required by the commissioner to be substantiated by an opinion of a bank, finance company, or other lending institution satisfactory to the commissioner. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-37 Registration; examination requirements. (a) Unless specifically exempt as provided in subsection (b), every applicant who is a natural person shall be required to pass a written examination in order to test the applicant's knowledge of the securities business. The passing score shall be seventy per cent.

(b) The examination requirement may be waived by proper showing or certification as to an applicant who:

- (1) Has been continuously registered by the SEC as an investment adviser as of January 1, 1983;
- (2) Has passed the SEC examination for investment advisers not more than two years immediately preceding the date of filing;
- (3) Has passed a specific examination or examinations for investment advisers given by the NASD;
- (4) Has passed a specific examination or examinations for investment advisers given by any national securities exchange;
- (5) Has passed the series seven general securities examination given by the NASD;
- (6) Has passed a specific examination or examinations for a chartered financial consultant (ChFC) and been designated as a chartered financial consultant; or
- (7) Has passed a specific examination or examinations for a chartered financial analyst (CFA) and been designated as a chartered financial analyst.

The fact that an applicant has passed an examination in another state or registered as an investment adviser in another state shall not exempt the applicant from the exam requirement.

(c) All applications for the examination shall be received together with the examination fee of \$100 at least forty-five days prior to the examination date. Examinations shall be administered semi-annually on the second Wednesday of March and September of each year in the examination room of the department of commerce and consumer affairs, 1010 Richards Street, Honolulu, Hawaii. Applicants who pass the examination and are otherwise qualified shall be registered as investment advisers upon receipt of the registration fee of \$50, which fee shall be paid within one hundred twenty days after notification that an applicant has passed the examination. Applicants who do not pay the registration fee within the one hundred twenty day period shall have their application canceled and shall have to file another application. Applicants who are unsuccessful in passing the examination may file an application for re-examination before the next closing date, together with the examination fee of \$100. Failure to pass this examination three times shall result in the denial of registration. Failure to pass the SEC examination three times shall result in the denial of registration. An

applicant may apply for examination after a one-year period after notification of the third failure to pass the examination.

(d) Any investment adviser whose registration has lapsed for two or more years before applying for registration shall be required to apply as a new applicant. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-38 Registration; disclosure statements. (a) An investment adviser shall deliver the separate disclosure statement required by section 485-25(c)(4), HRS, to an advisory client or prospective advisory client:

- (1) Not less than forty-eight hours prior to entering into any investment advisory contract with a client or prospective client; or
 - (2) At the time of entering into any contract, if the advisory client has a right to terminate the contract without penalty within five business days after entering into the contract; and
- (b) An investment adviser shall notify a client of any material changes affecting the disclosure statement or investment advisory contract within thirty days after the change has occurred. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §§485-14, 485-25)

§16-38-39 Registration; post-effective requirements. (a) Upon acceptance of the application by the commissioner, a certificate of registration shall be issued certifying that the investment adviser is authorized to engage in the investment advisory business in the State.

(b) Every registrant shall immediately notify the commissioner in writing of any material change in any information, exhibits, or schedules submitted, or circumstances disclosed in its last prior application, and a correcting amendment shall be filed at the time of occurrence or discovery of the changes, which include, but are not limited to the following:

- (1) Change in firm name, ownership, management, or control of an investment adviser;
- (2) A change in any of its partners, officers, or persons in similar positions;
- (3) Change in its business address, or the creation or termination of a branch office in Hawaii;
- (4) Change in type of entity, general plan, or character of dealer's business, method of operation or type of securities in which it is dealing or trading;
- (5) Material adverse change in financial condition, insolvency, dissolution or liquidation, or impairment of working capital, or

noncompliance with the minimum net worth or bond requirements hereinabove provided;

- (6) Termination of business or discontinuance of those activities as an investment adviser;
- (7) The filing of a criminal charge or civil action against a registrant or a partner, officer, or employee who acts as an investment adviser, in which a fraudulent, dishonest, or unethical act is alleged, or a violation of a securities law or any aspect of the securities business is involved; and
- (8) Entry of a court or administrative order or proceeding against a registrant to deny, suspend, or revoke a registration, or threatening to do so, or to enjoin it from engaging in or continuing any conduct or practice in the securities business, or to impose a fine, suspension, or expulsion from the NASD. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-40 Registration; expiration, renewal, termination. (a) All registrations shall automatically expire on December 31 of each odd-numbered year (unless sooner terminated) and shall be renewed not earlier than November 1 or later than December 1 of each odd-numbered year for the next two calendar years by filing the application for renewal, together with the renewal fees. Applications not received by December 1 shall be subject to a penalty of one hundred per cent of the renewal fee.

(b) Where registrations are permitted to expire without the filing of a renewal therefor, a subsequent application shall be considered in all respects as an original application.

(c) Registration may be terminated prior to the expiration date by filing a request for cancellation, together with the certificate of registration of an investment adviser and the certificates of registration of the investment adviser representatives. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-41 Books and records. (a) Every investment adviser shall make and keep the following books and records, which shall be maintained and preserved for a period of at least three years and made available for inspection by the commissioner upon reasonable notice. This chapter shall not require a member of a national securities exchange to make or keep the records of transactions cleared for a member by another member as are made and kept by the clearing member:

- (1) All partnership agreements, or all articles of incorporation, by-laws, minute books, and stock certificate books of the investment adviser;
- (2) A general ledger (or other records in the case of a sole proprietor) reflecting all asset, liability, income, expense, and capital accounts;
- (3) A record showing all payments received, including date of receipt, purpose, and from whom received; and all disbursements, including date paid, purpose, and to whom made;
- (4) A record showing all receivables and payables;
- (5) All trial balances, financial statements, and internal audit working papers which may be prepared relating to the business of the investment adviser;
- (6) All check books, bank statements, canceled checks and cash reconciliations of the investment adviser;
- (7) All bills or statements (or copies thereof), paid or unpaid, relating to the business of the investment adviser as such;
- (8) A memorandum of each order given by the investment adviser for the purchase or sale of any security of any instruction received by the investment adviser from the customer concerning the purchase, sale, receipt, or delivery of a particular security, and of any modification or cancellation of any order or instruction. The memoranda shall show the terms and conditions of the order, instruction, modification, or cancellation; shall identify the person connected with the investment adviser who recommended the transaction to the customer and the person who placed the order; and shall show the account for which entered, the date of entry, and the bank, broker, or dealer by or through whom executed. Orders entered pursuant to the exercise of discretionary power shall be so designated;
- (9) Copies of all written communications, correspondence, confirmations, appraisals, and other records relating to investment advice to customers;
- (10) Copies of all complaints of customers relating to investment activities for customers. In this paragraph, "complaint" means any written or oral statement of a customer or any person acting on behalf of a customer alleging a grievance involving the activities of persons under the control of the investment adviser in connection with providing investment advice or placing orders on behalf of customers;
- (11) A list or other record of all accounts in which the investment adviser is vested with any discretionary power with respect to the funds, securities, or transactions of any customer;

- (12) A copy of all powers of attorney and other evidences of the granting of any discretionary authority by any customer to the investment adviser or to a third party;
- (13) A copy of all written agreements entered into by the investment adviser with any customer, or with any other person if the agreement relates to the business of the investment adviser;
- (14) A copy of each notice, circular, advertisement, newspaper article, investment letter, bulletin, or other communication recommending the purchase or sale of a specific security, which the investment adviser circulates or distributes, directly or indirectly, to ten or more persons (other than investment supervisory clients or persons connected with the investment adviser), and if the notice, circular, advertisement, newspaper article, investment letter, bulletin or other communication does not state the reasons for the recommendation, a memorandum of the investment adviser indicating the reasons therefor; and
- (15) A record of every transaction in a security in which the investment adviser has, or by reason of the transaction acquires, any direct or indirect beneficial ownership, except:
 - (A) Transactions effected in any account over which neither the investment adviser nor any advisory representative of the investment adviser has any direct or indirect influence or control; and
 - (B) Transactions in securities which are direct obligations of the United States. The record shall state the title and amount of the security involved; the date and nature of the transaction (i.e., purchase, sale, or other acquisition or disposition); the price at which it was effected; and the name of the broker-dealer or bank with or through whom the transaction was effected. The record may also contain a statement declaring that the reporting or recording of any transaction shall not be construed as an admission that the investment adviser or advisory representative has any direct or indirect beneficial ownership in the security. A transaction shall be recorded not later than ten days after the end of the calendar quarter in which the transaction was effected.

(b) If a registered investment adviser has custody or possession of securities or funds of any client, the records required to be made and kept under subsection (a) shall include:

- (1) A journal or other record showing all purchases, sales, receipts, and deliveries of securities (including certificate numbers) for accounts and all other debits and credits to the accounts;
- (2) A separate ledger account for each client showing all purchases, sales, receipts, and deliveries of securities, the date and price of each purchase or sale, and all debits and credits;
- (3) Copies of confirmations of all transactions effected by or for the account of any client; and
- (4) A record for each security in which any client has a position, which record shall show the name of each client having any interest in the security, the amount of interest of each client, and the location of each security.

(c) Every registered investment adviser who renders any investment supervisory or management service to any client shall, with respect to the portfolio being supervised or managed and to the extent that the information is reasonably available to or obtainable by the investment adviser, make and keep true, accurate, and current:

- (1) Records showing separately for each client the securities purchased and sold, and the date, amount, and price of each purchase or sale;
- (2) For each security in which any client has a current position, information from which the investment adviser can promptly furnish the name of each client, and the current amount of the interest of the client; and
- (3) Any books or records required by this section may be maintained by the investment adviser in a manner that the identity of any client to whom the investment adviser renders investment supervisory services is indicated by numerical or alphabetical code or some similar designation.

(d) All books and records required to be made under the provisions of subsections (a) to (c) inclusive, of this section shall be maintained and preserved in an easily accessible place for a period of not less than three years from the end of the fiscal year during which the last entry was made on the record, the first two years in an appropriate office of the investment adviser.

(e) Charter documents, minute books, and stock certificate books of the investment adviser and of any predecessor, shall be maintained in the principal office of the investment adviser and preserved until at least three years after termination of the enterprise.

(f) A registered investment adviser, before ceasing to conduct or discontinuing business as an investment adviser, shall arrange for and be responsible for the preservation of the books and records required to be maintained and preserved under this section for the remainder of the period

specified in this section, and shall notify the commissioner in writing of the exact address where the books and records shall be maintained during the period.

(g) Books and records maintained under this section may be kept by means of photographic, photostatic, microfilm, microcard or other process which accurately reproduces the originals.

(h) Any book or other record made, kept, maintained, and preserved in compliance with provisions of this chapter, which is substantially the same as the book or other record required to be made, kept, maintained, and preserved under this section, shall satisfy the requirements of this section.

A record made and kept pursuant to any provision of subsection (a) which contains all the information required under any other provision of subsection (a), need not be maintained in duplicate in order to meet the requirements of the other provision of subsection (a).

(i) As used in this section, the terms "power of attorney" and "discretionary authority" do not include discretion as to the price at which or the time when a transaction is or is to be effected, if, before the order is given by the investment adviser, the client has directed or approved the purchase or sale of a definite amount of the particular security.

(j) An investment adviser pursuant to the minimum net worth and bond requirements of this section shall in addition to the records otherwise required under this section maintain a record of the proof of money balances of all ledger accounts in the form of trial balances and a record of the computation of net worth. The trial balances and computations shall be prepared currently at least quarterly.

(k) The commissioner may by order exempt any investment adviser from all or part of the requirements of this section, either unconditionally or upon specified conditions, if by reason of the special nature of its business, the commissioner finds that issuance of the order is necessary or appropriate in the public interest or for the protection of investors. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-16)

§16-38-42 Advertisements. (a) It shall constitute a fraudulent, deceptive, or manipulative act, practice or course of business within the meaning of section 485-25, HRS, for any investment adviser, directly or indirectly, to publish, circulate, or distribute any advertisement:

- (1) Which refers, directly or indirectly, to any testimonial of any kind concerning the investment adviser or concerning any advice, analysis, report, or other service rendered by the investment adviser; or

- (2) Which refers, directly or indirectly, to past specific recommendations of the investment adviser which were or would have been profitable to any person; provided that this shall not prohibit an advertisement which sets out or offers to furnish a list of all recommendations made by the investment adviser within the immediately preceding period of not less than one year if the advertisement, and list if it is furnished separately:
 - (A) State the name of each security recommended, the date and nature of each recommendation (e.g., whether to buy, sell, or hold), the market price at that time, the price at which the recommendation was to be acted upon, and the market price of each security as of the most recent practicable date; and
 - (B) Contain the following cautionary legend on the first page thereof in print or type as large as the largest print or type used in the body or text thereof: "It should not be assumed that recommendations made in the future will be profitable or will equal the performance of the securities in this list"; or
- (3) Which represents, directly or indirectly, that any graph, chart, formula, or other device being offered can in and of itself be used to determine which securities to buy or sell, or when to buy or sell them; or which represents directly or indirectly, that any graph, chart, formula, or other device being offered shall assist any person in making a decision as to which securities to buy, sell, or when to buy or sell them, without prominently disclosing in the advertisement the limitations thereof and the difficulties with respect to its use; or
- (4) Which contains any statement to the effect that any report, analysis, or other service shall be furnished free or without charge, unless the report, analysis, or other service actually is or shall be furnished entirely free and without any condition or obligation, directly or indirectly; or
- (5) Which contains any untrue statement of a material fact, or which is otherwise false or misleading.
- (b) For the purposes of this section the term "advertisement" shall include any notice, circular, letter, or other written communication addressed to more than one person, or any notice or other announcement in any publication or by radio or television, which offers:

- (1) Any analysis, report, or publication concerning securities, or which is to be used in making any determination as to when to buy or sell any security, or which security to buy or sell; or
- (2) Any graph, chart, formula, or other device to be used in making any determination as to when to buy or sell any security, or which security to buy or sell; or
- (3) Any other investment advisory service with regard to securities. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS §485-25)

SUBCHAPTER 12

INVESTMENT ADVISER REPRESENTATIVES

§16-38-48 Registration; generally. A person may be registered as an investment adviser representative under Chapter 485, HRS, if the commissioner finds that the applicant is of good repute and otherwise satisfies the requirements of chapter 485, HRS, and this chapter. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: Act 286, SLH 1985)

§16-38-49 Registration; eligibility requirements. (a) An applicant, if a natural person, shall have attained the age of eighteen years.

(b) An applicant shall be appointed by a registered investment adviser who shall state that the registered investment adviser believes the information in the application is true and complete.

(c) An investment adviser representative may not be registered with more than one investment adviser at any time. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: Act 286, SLH 1985)

§16-38-50 Registration; application. (a) An application for original or renewal registration shall be filed on a form prescribed by the commissioner or, in the case of an original application, on a form approved by the Securities and Exchange Commission and the State.

- (b) The application shall be filed together with the following:
 - (1) A filing fee of \$10;
 - (2) The applicant's photograph;

- (3) A copy of a written disclosure statement, as provided by section 485-25(c)(4), HRS, if the investment adviser representative engages in activities which are applicable under that section; and
- (4) Proof that the applicant has passed the exam requirement as provided by section 16-38-51, or otherwise qualifies for exemption from the exam as specified in section 16-38-51. The applicant shall specify the number of times of failure to pass the exam requirement provided by section 16-38-51 or the SEC examination.
- (c) Additional exhibits or information not specifically required by the application but essential to a full presentation of all material facts relating to applicant's qualification should be furnished properly identified.
- (d) The commissioner may make the examination of the applicant and require additional information deemed appropriate in consideration of the applicant's eligibility for registration.
- (e) An applicant for renewal of registration need not furnish the identical information schedules or exhibits submitted in connection with an original application, unless there has been a change in circumstances affecting previous disclosures or the data is specifically requested by the commissioner. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: Act 286, SLH 1985)

§16-38-51 Registration; examination requirements. (a) Unless specifically exempt as provided in subsection (b), every applicant who is a natural person shall be required to pass a written examination in order to test applicant's knowledge of the securities business. The passing score shall be seventy per cent.

(b) The examination requirement may be waived by proper showing or certification as to an applicant who:

- (1) Has been continuously registered by the SEC as an investment adviser as of January 1, 1983;
- (2) Has passed the SEC examination for investment advisers not more than two years immediately preceding the date of filing an application for registration;
- (3) Has passed a specific examination or examinations for investment advisers given by the NASD;
- (4) Has passed a specific examination or examinations for investment advisers given by any national securities exchange;
- (5) Has passed the series seven general securities examination given by NASD;
- (6) Has passed a specific examination or examinations for a chartered financial consultant (ChFC) and been designated as a chartered financial consultant; or

- (7) Has passed a specific examination or examinations for a chartered financial analyst (CFA) and been designated as a chartered financial analyst; or

The fact that an applicant has passed an examination in another state or registered as an investment adviser in another state shall not exempt the applicant from the exam requirement.

(c) All applications for the examination shall be received together with the examination fee of \$50 at least forty-five days prior to the examination date. Examinations shall be administered semi-annually on the second Wednesday of March and September of each year in the examination room of the department of commerce and consumer affairs, 1010 Richards Street, Honolulu, Hawaii. Applicants who pass the examination and are otherwise qualified shall be registered as investment adviser representative upon receipt of the registration fee of \$10, which fee shall be paid within one hundred twenty days after notification that an applicant has passed the examination. Applicants who do not pay the registration fee within the one hundred twenty day period shall have their application canceled and shall have to file another application. Applicants who are unsuccessful in passing the examination may file an application for reexamination before the next closing date, together with the examination fee of \$50. Failure to pass this examination three times shall result in the denial of registration. Failure to pass the SEC examination three times shall result in the denial of registration. An applicant may apply for examination after a one-year period after notification of the third failure to pass the examination.

(d) Any investment adviser representative whose registration has lapsed for two or more years before applying for registration shall be required to apply as a new applicant. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS Act 286, SLH 1985)

§16-38-52 Registration; disclosure statements. (a) An investment adviser representative shall deliver the separate disclosure statement required by section 485-25(c)(4), HRS, to an advisory client or prospective advisory client:

- (1) Not less than forty-eight hours prior to entering into any investment advisory contract with a client or prospective client; or
- (2) At the time of entering into any contract, if the advisory client has a right to terminate the contract without penalty within five business days after entering into the contract.

(b) An investment adviser representative shall notify a client of any material changes affecting the disclosure statement or investment advisory contract within thirty days after the change has occurred. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: Act 286, SLH 1985)

§16-38-53 Registration; post-effective requirements. (a) Upon completion of the application, compliance with the examination requirement, and acceptance by the commissioner, registration shall become effective and a certificate of registration (white copy) shall be issued certifying the authority for the investment adviser representative to engage in the investment advisory business on behalf of the investment adviser designated thereon. The blue copy of the certificate shall be retained by the investment adviser employer.

(b) The representative's certificate of registration shall be carried by the applicant at all times when engaged in the investment advisory business and shall be presented upon request.

(c) Every applicant or registrant shall immediately notify the commissioner of the filing of a criminal charge or civil action in which a fraud, dishonest, or unethical action is alleged or a violation of securities law is involved. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: Act 286, SLH 1985)

§16-38-54 Registration; expiration, renewal, termination. (a) All registrations shall automatically expire on December 31 of each odd-numbered year, unless sooner terminated, and shall be renewed by the investment adviser employing the representative not earlier than November 1 or later than December 1 of each odd-numbered year for the next two calendar years by filing an application for renewal of investment adviser representative together with the renewal fee. Applications not received by December 1 shall be subject to a penalty of one hundred per cent of the renewal fee.

(b) Where registrations are permitted to expire without the filing of a renewal therefor, a subsequent application shall be considered in all respects as an original application.

(c) An investment adviser representative's certificate of registration may be terminated prior to its expiration date by the investment adviser employing the investment adviser representative. An investment adviser may terminate the registration of any representative by filing a notice of termination, in writing, with the commissioner together with the representative's certificate of registration (white copy).

(d) An investment adviser representative's certificate of registration shall not be transferred. When a representative terminates connection with an investment adviser with whom the representative is registered, and wishes to be employed by another investment adviser, a notice of termination shall be filed with the commissioner together with the representative's certificate of registration (white copy). The representative may then reapply for registration with the new

investment adviser by filing an appropriate form. The form shall be endorsed by the new investment adviser.

(e) Termination of any investment adviser's registration for any reason shall automatically constitute cancellation of all investment adviser representatives registered thereunder.

(f) When an investment adviser representative ceases those activities of a representative, or the representative otherwise becomes ineligible to be registered, notice shall be promptly filed by the investment adviser with whom the subject is registered and the representative's certificate of registration shall be surrendered to the commissioner. In no event shall the notice be later than ten days following the event or occurrence. The notice shall be in letter form. [Eff and comp 10/12/85] (Auth: HRS §485-2) (Imp: HRS Act 286, SLH 1985)

SUBCHAPTER 13

FINES AND PENALTIES

§16-38-58 Fines and penalties. Any fines and penalties imposed under this chapter shall be deposited into the compliance resolution fund. [Eff and comp 10/12/85] (Auth: HRS §§485-2, 26-9) (Imp: HRS §§485-15, 485-21)

Amendments to and compilation of Chapter 16-38, Hawaii Administrative Rules, on the Summary page dated July 18, 1985, were adopted on July 18, 1985, following public hearing held on July 18, 1985, after public notice was given in the Honolulu Advertiser on June 27, 1985.

They shall take effect ten days after filing with the Office of the Lieutenant Governor.

/s/ Russel S. Nagata
RUSSEL S. NAGATA
Director of Commerce and Consumer Affairs

/s/ George R. Ariyoshi
GEORGE R. ARIYOSHI
Governor
State of Hawaii

Dated: 10-1-85

October 2, 1985
Filed

APPROVED AS TO FORM:

/s/ Clifford K. Higa
Deputy Attorney General

DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS

Amendment and Compilation of Chapter 16-38
Hawaii Administrative Rules

July 18, 1985

SUMMARY

1. Title amended.
2. §§16-38-1 to 16-38-5 are amended.
3. §§16-38-5.1 to 16-38-5.6 are amended and renumbered.
4. §16-38-6 is amended.
5. §§16-38-6.1 to 16-38-6.5 are amended and renumbered.
6. §§16-38-7 to 16-38-11 are amended.
7. §§16-38-11.1 to 16-38-11.9 are amended and renumbered.
8. §16-38-12 is repealed.
9. §§16-38-14 to 16-38-18 are amended.
10. §16-38-20 is amended.
11. A new subchapter 10 (§§16-38-21 to 16-38-29) is added.
12. A new subchapter 11 (§§16-38-33 through 42) is added.
13. A new subchapter 12 (§§16-38-48 through 54) is added.
14. A new subchapter 14 (§16-38-58) is added.
15. Chapter 38 is compiled.

§16-38-3 Fees. The following fees shall be submitted with the application:

- (1) The fee for registration of securities by qualification shall be one-tenth of one per cent of the aggregate offering price of the securities to be offered in the State; minimum, \$50; maximum, \$500; renewal, \$50;
- (2) The fee for registration of securities by notification shall be one-twentieth of one per cent of the aggregate offering price of the securities to be offered in the State; maximum, \$250;
- (3) The fee for registration of dealers shall be \$100 (original and renewal);
- (4) Registration by investment advisers shall be \$100 (original and renewal);
- (5) The fee for registration of securities salesperson shall be \$25 (original, reapplication, and renewal);
- (6) The fee for the securities salesperson examination shall be \$50;
- (7) The fee for registration of investment adviser representatives shall be \$25 (original, reapplication, and renewal);
- (8) The fee for the investment adviser representative examination shall be \$50;
- (9) The fee for the investment adviser examination shall be \$250; and
- (10) The fee for copies of documents filed in the office of the commissioner shall be 25 cents per page. [Eff 6/4/70; am 5/27/80; am and ren §16-38-3, 7/30/81; am and comp 10/12/85; am 4/4/87] (Auth: HRS§485-2) (Imp: HRS §§485-9, 485-10,485-11, 485-14)

§16-38-5.2 Registration; application. * * *

(b) The application shall be filed together with the filing fee of \$100 and consent to service of process, \$5,000 bond, or cash or securities in lieu thereof, a verified balance sheet as of a date within thirty days of filing, or if the applicant has been engaged in business one year or more preceding, a balance sheet certified by and independent public accountant as of the last fiscal year, together with a balance sheet verified by the applicant as of a date within thirty days of filing.

* * *

[Eff 6/4/70; am 1/1/71; am and ren §16-38-5, 7/30/81; am, ren §16-38-5.2 and comp 10/12/85; am 4/4/87] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-6.3 Registration; examination requirements. * * *

(f) Applications submitted by applicants of non-NASD member firms or applicants of issuers (Oahu applicants only) shall be received together with the part I examination fee of \$50 by the respective closing dates. Examinations shall be given in the examination room of the department of commerce and consumer affairs, 1010 Richards Street, Honolulu, Hawaii. Dealers and issuers shall be notified by letter of the grades received by their applicants. Applicants who pass the examination and are otherwise qualified shall be registered as securities salespersons upon receipt of the registration fee of \$25, which shall be paid within one hundred twenty days after notification that an applicant has passed the examination. Applicants who do not pay the registration fee within the one hundred twenty day period shall have their application canceled and shall file another application. Applicants who are unsuccessful in passing the examination may file an application for re-examination before the next closing date, together with the examination fee of \$50. The part I score shall only be valid for a period of two years.

(g) Applicants of non-NASD member firms or applicants of issuers who reside on the neighbor islands may take the part I examination on their respective islands and the examination dates shall be set after the application is filed. The requirements listed in subsection (f) pertaining to the payment of the registration fee shall also apply to applicants who reside on the neighbor islands.

(h) Applicants who have passed the NASD examination shall submit a copy of the "Notice of Acceptance" sent to the dealer by the NASD. Applicants who have passed the USASLE examination shall submit a copy of notification of grade results and certificate, on a form provided by the commissioner, stating that they have read and understand chapter 485, HRS, and this chapter.

(i) Applicants who subsequently pass both examinations and are otherwise qualified shall be registered as securities salespersons upon receipt of the registration fee of \$25 which shall be paid within one hundred twenty days after notification that they have passed both examinations. Applicants who do not pay the registration fee within the one hundred twenty day period shall have their applications canceled and shall file new applications and meet all licensure requirements.

* * *

[Eff 6/4/701; am 5/27/80; am and ren §16-38-6, 7/30/81; am 11/5/81; am, ren §16-38-6.3 and comp 10/12/85; am 4/4/87] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-7 Denial, suspension, and revocation. * * *

(b) Without in any way limiting the generality thereof, for the purposes of section 485-15(11), HRS, any of the following shall demonstrate an applicant's or registrant's unworthiness to transact business of a dealer or salesperson:

- (1) Causing unreasonable delay or failure to execute orders, liquidate customers' accounts, or in making delivery of securities purchased or remittances (or credit) for securities sold;
- (2) Selling securities at unfair prices in relation to market value, or with unreasonable or excessive markups or commissions;
- (3) Effecting transactions in the account of a customer without the customer's knowledge or consent or maintaining discretionary accounts without written authorization;
- (4) Wilful switching, churning, overtrading, or reloading of securities in a customer's account for the ostensible purpose of accumulating or compounding commissions;
- (5) Inducing a customer to invest beyond the customer's known immediate financial resources, or without regard to the nature and character of the account;
- (6) Engaging or aiding in "boiler room" operations or high-pressure tactics in connection with the promotion of speculative offerings or "hot-issues" by means of an intensive telephone campaign or unsolicited calls to persons not known by, or having an account with the salesperson or dealer represented by the applicant, whereby the prospective purchaser is encouraged to make a hasty decision to buy, irrespective of the prospective purchaser's investment needs and objectives;
- (7) Participating in the solicitation or offer for sale of promotional securities without the use and dissemination of a prospectus (where required), or making oral or written statements contrary to or inconsistent with the disclosures contained therein;
- (8) Making false, misleading, deceptive, exaggerated, or flamboyant representations or predictions in the solicitation or sale of a security;
 - (A) That the security shall be resold or repurchased; or
 - (B) That the security shall be listed or traded on an exchange or established market; or
 - (C) That the security shall result in an assured, immediate or extensive increase in value, future market price, or return on investment; or
 - (D) With respect to the issuer's financial condition, anticipated earnings, potential growth, or success; or
 - (E) That there is a guarantee against risk or loss;

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- (9) Failing to disclose a dual agency capacity or effecting transactions upon terms and conditions other than those stated per confirmations;
- (10) Failing to make a bona fide public offering pursuant to an underwriting agreement or entering into an arrangement which establishes unfair or unreasonable terms and conditions or compensation;
- (11) Establishing fictitious accounts in order to execute transactions which would otherwise be prohibited;
- (12) Entering into agreements for selling concessions, discounts, commissions, or allowances as consideration for services in connection with the distribution or sale of a security in Hawaii to any non-licensed dealer or salesperson, unless the person is not required to be registered in order to engage in the securities business in this State;
- (13) Operating a securities business while being unable to meet current liabilities, or violating any rule or order relating to minimum capital, bond, record-keeping and reporting requirements, or provision concerning use, commingling, or hypothecation of customers' funds or securities; or
- (14) Failure or refusal to furnish a customer, upon reasonable request, information to which the customer is entitled, or to respond to a formal written demand or complaint.

* * *

[Eff 6/4/70; am and ren §16-38-7, 7/30/81; am and comp 10/12/85; am 4/4/87] (Auth: HRS §485-2) (Imp: HRS §485-15)

§16-38-16 Renewals. The registration statement may be renewed not less than fifteen days prior to the expiration date by filing a new prospectus containing information of a date not more than ninety days prior to the date of filing, together with the renewal fee of \$50. The front cover shall show the balance of the offering, the amount of the original registration, and the date the original registration became effective. [Eff 6/4/70; am and ren §16-38-16, 7/30/81; am and comp 10/12/85; am 4/4/87] (Auth: HRS §485-2) (Imp: HRS §§485-10, 485-11)

§16-38-23 Filing. (a) The issuer shall file with the commissioner a signed copy of Form D (17 CFR 230.500) and State registration form, not later than ten days after the first offer is made in the State.

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[Eff and comp 10/12/85; am 4/4/87] (Auth: HRS §485-2) (Imp: HRS §485-6)

§16-38-35 Registration; application. * * *

- (b) The application shall be filed together with the following:
- (1) A filing fee of \$100;
 - (2) Consent to service of process;
 - (3) If the applicant is a natural person, the applicant's photograph;
 - (4) A copy of a written disclosure statement, as provided by section 485-25(c)(4), HRS, if the adviser engages in activities which are applicable under that section;
 - (5) A \$50,000 bond or cash or securities in lieu thereof if the adviser retains custody or possesses discretionary authority over clients' money, securities, or other assets; or a \$5,000 bond or cash or securities in lieu thereof if the adviser does not retain custody or possess such authority;
 - (6) A balance sheet as of a date within thirty days of filing, or if applicant has been engaged in business one year or more preceding, a balance sheet certified by an independent public accountant as of the last fiscal year, together with a balance sheet verified by the applicant as of a date within thirty days of filing. However, if the applicant does not have custody or discretionary authority over client funds, the adviser need only file financial statements verified by the adviser;
 - (7) A certificate of insurance covering the adviser's business for errors and omissions, as specified by section 16-38-34; and
 - (8) Proof that the applicant has passed the exam requirement as provided by section 16-38-37, or otherwise qualifies for exemption from the exam as specified in section 16-38-37. The applicant shall specify the number of times of failure to pass the exam requirement provided by section 16-38-37 or the SEC examination.

* * *

[Eff and comp 10/12/85; am 4/4/87] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-37 Registration; examination requirements. (a) Unless specifically exempt as provided in subsection (b), every applicant who is a natural person or a partnership whose general partners are natural persons shall pass a written examination in order to test the applicant's knowledge of the securities business. The passing score shall be seventy per cent.

(b) The examination requirement may be waived by proper showing or certification as to an applicant who:

- (1) Has been continuously registered by the SEC as an investment adviser as of January 1, 1983;
- (2) Has passed the SEC examination for investment advisers not more than two years immediately preceding the date of filing an application for registration;
- (3) Has passed a specific examination or examinations for investment advisers given by the NASD;
- (4) Has passed a specific examination or examinations for investment advisers given by any national securities exchange;
- (5) Has passed the series one securities examination given by the NASD, provided that the applicant has been continuously licensed with a securities broker-dealer or investment adviser since passing the examination;
- (6) Has passed the series seven general securities examination given by the NASD not more than two years immediately preceding the date of filing an application for registration or has passed the series seven general securities examination given by the NASD, provided that the applicant has been continuously licensed with a securities broker-dealer or investment adviser since passing the examination;
- (7) Has passed a specific examination or examinations for a chartered investment consultant (CIC) and been designated as a chartered investment consultant; or
- (8) Has passed a specific examination or examinations for a chartered financial analyst (CFA) and been designated as a chartered financial analyst.

The fact that an applicant has passed an examination in another state or registered as an investment adviser in another state shall not exempt the applicant from the exam requirement.

(c) All applications for the examination shall be received together with the examination fee of \$250 at least forty-five days prior to the examination date. Examination shall be administered semi-annually on the second Wednesday of March and September of each year in the examination room of the department of commerce and consumer affairs, 1010 Richards Street, Honolulu, Hawaii. Applicants who pass the examination and are otherwise qualified shall be registered as investment advisers upon receipt of the registration fee of \$100, which fee shall be paid within one hundred twenty days after notification that an applicant has passed the examination.

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Applicants who do not pay the registration fee within the one hundred twenty day period shall have their application canceled and shall have to file another application. Applicants who are unsuccessful in passing the examination may file an application for re-examination before the next closing date, together with the examination fee of \$100. Failure to pass this examination three times shall result in the denial of registration. Failure to pass the SEC examination three times shall result in the denial of registration. An applicant may apply for examination after a one-year period after notification of the third failure to pass the examination. [Eff and comp 10/12/85; am 4/4/87] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-40 Registration; expiration, renewal, termination. * * *

(c) Registration may be terminated prior to the expiration date by filing a request for cancellation, together with the certificate of registration of an investment adviser and the certificates of registration of the investment adviser representatives. [Eff and comp 10/12/85; am 4/4/87] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-50 Registration; application. * * *

- (b) The application shall be filed together with the following:
- (1) A filing fee of \$25;
 - (2) The applicant's photograph;
 - (3) A copy of a written disclosure statement, as provided by section 485-25(c)(4), HRS, if the investment adviser representative engages in activities which are applicable under that section; and
 - (4) Proof that the applicant has passed the exam requirement as provided by section 16-38-51, or otherwise qualifies for exemption from the exam as specified in section 16-38-51. The applicant shall specify the number of times of failure to pass the exam requirement provided by section 16-38-51 or the SEC examination.

* * *

[Eff and comp 10/12/85; am 4/4/87] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-51 Registration; examination requirements. (a) Unless specifically exempt as provided in subsection (b), every applicant who is a natural person shall be required to pass a written examination in order to test applicant's knowledge of the securities business. The passing score shall be seventy per cent.

(b) The examination requirement may be waived by proper showing or certification as to an applicant who:

- (1) Has been continuously registered by the SEC as an investment adviser as of January 1, 1983;
- (2) Has passed the SEC examination for investment advisers not more than two years immediately preceding the date of filing an application for registration;
- (3) Has passed a specific examination or examinations for investment advisers given by the NASD;
- (4) Has passed a specific examination or examinations for investment advisers given by any national securities exchange;
- (5) Has passed the series one securities examination given by the NASD, provided that the applicant has been continuously licensed with a securities broker-dealer or investment adviser since passing the examination;
- (6) Has passed the series seven general securities examination given by NASD not more than two years immediately preceding the date of filing an application for registration, or has passed the series seven general securities examination given by the NASD, provided that the applicant has been continuously licensed with a securitiesbroker-dealer or investment adviser since passing the examination;
- (7) Has passed a specific examination or examinations for a chartered investment consultant (CIC) and been designated as a chartered investment consultant; or
- (8) Has passed a specific examination or examinations for a chartered financial analyst (CFA) and been designated as chartered financial analyst.

The fact that an applicant has passed an examination in another state or registered as an investment adviser in another state shall not exempt the applicant from the exam requirement.

(c) All applications for the examination shall be received together with the examination fee of \$50 at least forty-five days prior to the examination date. Examinations shall be administered semi-annually on the second Wednesday of March and September of each year in the examination room of the department of commerce and consumer affairs, 1010 Richards Street, Honolulu, Hawaii. Applicants who pass the examination and are otherwise qualified shall be registered as investment adviser representative upon receipt of the registration fee of \$25, which fee shall be paid within one hundred twenty days after notification that an applicant has passed the examination. Applicants who do not pay the

registration fee within the one hundred twenty day period shall have their application canceled and shall have to file another application. Applicants who are unsuccessful in passing the examination may file an application for reexamination before the next closing date, together with the examination fee of \$50. Failure to pass this examination three times shall result in the denial of registration. Failure to pass the SEC examination three times shall result in the denial of registration. An applicant may apply for examination after a one-year period after notification of the third failure to pass the examination.

(d) Any investment adviser representative whose registration has lapsed for two or more years before applying for registration shall be required to apply as a new applicant. [Eff and comp 10/12/85; am 4/4/87] (Auth: HRS §485-2) (Imp: HRS §485-14)

§16-38-54 Registration; expiration, renewal, termination. * * *

"(b) Where registrations are permitted to expire without the filing of a renewal therefor, a similar application may be filed not later than two years after the date of expiration on the form entitled, "Reapplication for Registration of Investment Adviser Representative" which is marked Appendix A, location at the end of this chapter, and made a part of this section. Applications filed after two years from the expiration or termination date shall be considered as original applications.

* * *

[Eff and comp 10/12/85; am 4/4/87] (Auth: HRS §485-2) (Imp: HRS §485-14)

DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS

Amendments to chapter 16-38, Hawaii Administrative Rules, on the Summary page dated January 19, 1987, were adopted on January 19, 1987, following a public hearing held on January 19, 1987, after notice was given in the Honolulu Advertiser on December 29, 1986.

These amendments shall take effect ten days after filing with the Office of the Lieutenant Governor.

/s/ Robert A. Alm

ROBERT A. ALM

Director of Commerce and Consumer Affairs

/s/ John Waihee

JOHN WAIHEE

Governor

State of Hawaii

Dated: March 25, 1987

March 25, 1987

Filed

APPROVED AS TO FORM:

/s/ Clifford K. Higa

Deputy Attorney General

DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS

Chapter 16-36 and 16-38, Hawaii Administrative Rules, which were adopted on January 19, 1987 and became effective on April 4, 1987, were the subject of another opportunity to provide public comment. A public hearing was held on September 12, 1989 at 8:00 a.m. in the Kuhina Nui Room, Department of Commerce and Consumer Affairs. Public notice of the hearing was published on August 2, 1989 in the Advertiser, Star-Bulletin, West Hawaii Today, the Maui News, the Hawaii Tribune-Herald, and the Garden Island.

After review of the comments submitted, the Department of Commerce and Consumer Affairs determined that the rules should remain as originally adopted.

/s/ Robert A. Alm

ROBERT A. ALM

Director

Department of Commerce and Consumer Affairs

September 14, 1989

Date

DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS

Amendments to Chapter 16-38
Hawaii Administrative Rules

January 19, 1987

SUMMARY

1. §16-38-3 is amended.
2. §16-38-5.2 is amended.
3. §16-38-6.3 is amended.
4. §16-38-7 is amended.
5. §16-38-16 is amended.
6. §16-38-23 is amended.
7. §16-38-35 is amended.
8. §16-38-37 is amended.
9. §16-38-40 is amended.
10. §16-38-50 is amended.
11. §16-38-51 is amended.
12. §16-38-54 is amended.